

Stephen David Prowse, Ph.D.

New York, NY

March 5, 2010

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1 UNITED STATES DISTRICT COURT
2 FOR THE SOUTHERN DISTRICT OF NEW YORK
3 -----
4 SECURITIES AND EXCHANGE COMMISSION,
5 Plaintiff,
6 v.
7 ANDREAS BADIAN, et al.,
8 Defendants.

9

10 CIVIL ACTION NO. 06-CV-2621 LTS (DFE)

11 -----

12 VIDEOTAPED DEPOSITION OF
13 STEPHEN DAVID PROWSE, Ph.D.

14 March 5, 2010

15

16 T R A N S C R I P T of the deposition
17 taken before BRIDGET LOMBARDOZZI, a Certified
18 Shorthand Reporter, CRR, RMR, RPR, and Notary
19 Public of the State of New York, at the
20 offices the SECURITIES AND EXCHANGE COMMISSION,
21 3 World Financial Center, New York, New York,
22 on March 5, 2010, commencing at 10:07 a.m.

23

24 Reported by:

25 Bridget Lombardozzi, CSR, RMR, CRR, CLR

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1	APPEARANCES:	1	PREVIOUSLY MARKED EXHIBITS (continued):
2	SECURITIES AND EXCHANGE COMMISSION	2	EXHIBIT 86 Page 210
3	Attorneys for the Plaintiff	3	EXHIBIT 87 Page 210
4	100 F Street N.E.	4	EXHIBIT 88 Page 210
5	Washington, D.C. 20549	5	EXHIBIT 89 Page 210
6	202.551.4480	6	EXHIBIT 90 Page 210
7	BY: KENNETH J. GUIDO, ESQUIRE	7	EXHIBIT 10 Page 220
8		8	EXHIBIT 57 Page 241
9	DLA PIPER LLP (US)	9	EXHIBIT 47 Page 242
10	Attorneys for Defendant Andreas Badian	10	
11	and the Witness	11	
12	1251 Avenue of the Americas	12	
13	New York, New York 10020-1104	13	
14	212.335.4892	14	
15	BY: JOSHUA S. SOHN, ESQUIRE	15	
16	CARYN G. SCHECHTMAN, ESQUIRE	16	
17	MEGAN VESELY, ESQUIRE	17	
18		18	
19	ALSO PRESENT:	19	
20	FREDERICK C. DUNBAR, US SEC	20	
21	LAWRENCE R. GLOSTEN	21	
22	CHARLES M. JONES	22	
23	JONATHAN CLAY, Videographer	23	
24		24	
25		25	
	Page 3		Page 5
1	INDEX	1	* March 5, 2010 *
2	Witness Page	2	THE VIDEOGRAPHER: Good morning.
3	STEPHEN DAVID PROWSE, Ph.D.	3	We are now on the record in the matter of
4	By Mr. Guido 6	4	Securities and Exchange Commission versus
5		5	Badian. Today's date is Friday, March the 5th,
6	EXHIBITS	6	2010. The time is 10:07 a.m.
7	I.D. Description Page	7	This is the video recorded
8	BP-21 11/4/09 Retention Letter for	8	deposition of Mr. Stephen Prowse being taken at
9	FTI Consulting to DLA Piper 7	9	3 World Financial Center located in New York
10	BP-22 Subpoena for Mr. Prowse 104	10	City.
11	BP-23 Exhibit 13B - Regression Analysis 95	11	I am the camera operator. My name
12	BP-24 Exhibit 13B - Regression Analysis 106	12	is Jonathan Clay, in association with Alderson
13	BP-25 DS Pet Quarters Random Notes 223	13	Reporting. The court reporter is Bridget
14	BP-26 Confidence Intervals - 4 pages 281	14	Lombardozzi, also in association with Alderson
15	BP-27 "Death Spiral Convertibles"	15	reporting.
16	Article by Hillion and Vermaelen 320	16	Will all the attorneys please
17	BP-28 "What's Wrong with Bonferroni	17	identify themselves and the parties they
18	Adjustments" article by Perneger 324	18	represent, beginning with the party noticing
19		19	this proceeding.
20	PREVIOUSLY MARKED EXHIBITS:	20	MR. GUIDO: Kenneth Guido
21	EXHIBIT 4 Page 9	21	representing the Securities and Exchange
22	EXHIBIT 14 Page 43	22	Commission. I'm accompanied by Larry Glosten
23	EXHIBIT 12 Page 158	23	and Charles Jones and Fred - Fred Dunbar.
24	EXHIBIT 15 Page 171	24	MR. SOHN: Joshua Sohn from DLA
25	EXHIBIT 5 Page 196	25	Piper with Caryn Schechtman and Megan Vesely.

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 THE VIDEOGRAPHER: Will the court	2 you wish to use to refer to it. But I will be
3 reporter please administer the oath.	3 referring to Badian's trading.
4 S T E P H E N D A V I D	4 So if you want to each time
5 P R O W S E , Ph.D., FTI Consulting, 2001 Ross	5 clarify that in your view it's Rhino trading,
6 Avenue, Ste 400, Dallas, Texas, having been	6 I'm perfectly happy for you to do so.
7 duly sworn, testified as follows:	7
8 DIRECT-EXAMINATION	8 But my question was: Were you
9 BY MR. GUIDO:	9 retained to do an -- a study of Badian's
10 Q. Will you state your full name for	10 trading of Sedona stock?
11 the record, please?	11 A. I was retained in this matter to
12 A. Stephen David Prowse.	12 do a study of Rhino's trading of Sedona stock,
13 Q. Where are you employed?	13 yes, understanding that clarification.
14 A. I'm employed at a company called	14 Q. Now -- and prior to that time, you
15 FTI Consulting.	15 had not examined the trading in Sedona stock?
16 Q. How long have you been there?	16 A. Prior to that time, I had not done
17 A. I've been at FTI Consulting since	17 any examination of trading in Sedona stock.
18 November of 2003.	18 Q. And what did you do after you were
19 Q. Were you retained to be an expert	19 retained on November 4th, 2009, to prepare for
20 in this litigation?	20 the expert report that you provided in this
21 A. Yes.	21 case?
22 MR. GUIDO: I'd like to have the	22 A. Well, Mr. Beloreshki and I were
23 court reporter hand you what I've marked as	23 hired as joint experts in this matter. So
24 Exhibit No. 21. It's a premarked exhibit. The	24 after I was retained, I discussed with him the
25 court reporter has it.	25 matter and the appropriate approach to answer
Page 7	
1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 THE REPORTER: I gave it back to	2 And based on our -- our discussion
3 you, sir.	3 with -- based on my discussion with him, we
4 MR. GUIDO: She did, and I don't	4 proceeded to perform the analysis.
5 have it.	5 Q. Okay. Will you take a look at --
6 MR. SOHN: Mark this one.	6 in front of you in the blue batch are the
7 (Whereupon, exhibit is received and	7 exhibits from Mr. Beloreshki's deposition.
8 marked BP-21 for identification.)	8 I'll be using them in this deposition.
9 BY MR. GUIDO:	9 And I'd like you to take a look at
10 Q. Is Exhibit 21 the letter of	10 Exhibit No. 4.
11 retention that you signed on November 4th,	11 MR. JONES: I think it's not on
12 2009, to appear as an expert witness in this	12 top.
13 matter?	13 MR. SOHN: Number 1's on top.
14 MR. SOHN: Objection to form.	14 MR. JONES: You're good.
15 A. Yes, this is the one I signed.	15 (Whereupon, there is a pause in
16 Q. Now, prior to November 4th, 2009,	16 the proceedings.)
17 had you done any work with regard to the	17 BY MR. GUIDO:
18 Sedona's trading -- I mean the trading by	18 Q. Have you had a chance to review
19 Andreas Badian in the Sedona stock?	19 Exhibit No. 4?
20 A. I have not done any work with	20 A. Yes.
21 regards to Rhino trading in Sedona stock prior	21 Q. Okay. Is that the expert report
22 to being retained on this matter.	22 that you prepared in this matter?
23 Q. For definitional purposes for the	23 A. Yes, it is.
24 record, I'll be referring to Badian's trading	24 Q. Okay. Now, what documents did you
25 and you're perfectly free to use whatever term	25 review prior to signing this report? I think

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1 - STEPHEN D. PROWSE - 2 the date is November 24th? 3 A. November 24th, correct. 4 Q. What documents did you review? 5 A. The documents I reviewed, I 6 believe, would be listed in Exhibit 3. These 7 would be documents I directly reviewed, or the 8 team that was working on the engagement 9 reviewed. 10 Q. Pardon? 11 A. The team that was working on the 12 engagement reviewed. 13 Q. I asked what you reviewed. 14 A. I reviewed -- I reviewed the 15 Complaint; I reviewed the responses and 16 objections, and the first supplemental 17 responses and objections; I reviewed the audit 18 trail reports. I believe I reviewed some of 19 these individual numbered Bates documents, if 20 not all of them. I reviewed the trading data 21 which was in electronic format. And I may 22 have reviewed some of these account statements. 23 I reviewed the Chaplinsky and Haushalter 24 article. 25 Q. Pardon?	1 - STEPHEN D. PROWSE - 2 Q. Can you tell us what literature 3 that is? 4 A. There's a Hillion and Vermaelen 5 article that would have appeared, I believe, in 6 the Journal of Financial Economics. There is 7 Mr. Beloreshki's article. There is -- 8 Q. What article is that? 9 MR. SOHN: Mr. Guido, can you 10 please let the witness finish? 11 MR. GUIDO: I'm sorry. 12 A. That is the article that you 13 questioned him about on Tuesday, I believe. 14 Q. The one that you co-authored 15 with -- 16 A. Yes. 17 Q. -- Mr. Beloreshki? 18 A. Yes. 19 There may be -- there may be other 20 articles that are on the broad topic of PIPEs 21 or future price securities out there that I 22 have read before, but I can't -- they don't 23 come to mind as I sit here. 24 Q. Well, when you were sitting there 25 and you were preparing the report, did they
Page 11	Page 13
1 - STEPHEN D. PROWSE - 2 A. I reviewed the Chaplinsky and 3 Haushalter article. And I reviewed various 4 data from Bloomberg, from FactSet, from the 5 NBER, and reviewed various SEC filings. 6 Q. Well, let me ask you something: 7 How did you obtain the Chaplinsky article to 8 review? 9 A. I can't remember. I may have had 10 it. I may individually have had it, a hard 11 copy of it. 12 Q. What is your understanding of the 13 subject matter of that paper? 14 A. That it looks at -- it examines 15 the financial characteristics of certain -- of 16 PIPEs, private investments in public equity, 17 and looks at the characteristics of firms that 18 are issuing them and performs some -- a variety 19 of economic tests. And -- 20 Q. Did you review any other 21 literature that covered that subject matter? 22 A. For this particular engagement, 23 no. I'm aware of other literature out there 24 that talks about the -- similar to the 25 Chaplinsky and Haushalter article.	1 - STEPHEN D. PROWSE - 2 come to mind? 3 A. I didn't review them specifically 4 for the report, but my body of knowledge that 5 is -- that has been accumulated over 25 years 6 doing economics, or longer, it's -- it's just 7 sitting there as general awareness and general 8 knowledge of what the literature says and 9 what -- what some people have written. 10 Q. Okay. Let's take Mr. Beloreshki's 11 article. Okay? 12 A. Uh-huh. 13 Q. In his article, does he address 14 the question of the motivation of people that 15 bring lawsuits contending that the prices of 16 stock have been manipulated? 17 A. Does he address the motivation of 18 people bringing lawsuits? 19 Q. Alleging market manipulation. 20 A. He may talk about that. 21 Q. Well, what did he say? 22 A. I can't recall specifically what 23 he said. 24 Q. What about -- 25 A. I'd be happy to look at the

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	article if you want me to.	2	Q. Do you know?
3	Q. We'll have to look at the	3	A. I haven't done a study of what FTI
4	article?	4	has issued in terms of financing their
5	A. I'd be happy to if you want me to	5	activities. I know they're buying back stock
6	look at it.	6	just from my general knowledge, so...
7	Q. No, I understand that. You'd be	7	It would be extremely surprising
8	happy to look at the article.	8	to me if they had issued an FPS, as I
9	A. Yeah.	9	understand what an FPS is. But I wouldn't be
10	Q. And what about Hildebrand? What	10	surprised maybe if they issued a convertible
11	did they say about the motivations of people	11	bond.
12	who allege market manipulation?	12	Q. What do you understand an FPS
13	A. Hildebrand?	13	is?
14	Q. I think it was --	14	A. A future -- well, FPSs can be
15	A. I'm not aware of the person you	15	customized -- they're customized securities
16	said, Hildebrand.	16	between, you know, sophisticated entities. So
17	Q. I'm sorry. You mentioned -- I	17	their terms can vary a lot. But, generally, I
18	thought that you said Hildebrand.	18	would describe a future price security as a
19	What was the -- what was the other	19	convertible note that is convertible after some
20	article that you said that you were aware of?	20	lock-up period into the equity of the firm
21	A. There were two authors: One	21	issuing the bond or issuing the note at some
22	was -- one's surname is Hillion.	22	discount to a -- to a benchmark price that's
23	Q. Hillion, excuse me.	23	calculated based on some -- some measure of the
24	A. H-i-l-l-i-o-n. And the other's	24	current stock price of the firm.
25	surname Vermaelen, V-e-r-m-a-e-l-e-n, I think.	25	Q. Now, when you reviewed the -- or
	Page 15		Page 17
1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	They're telling me I got that right.	2	when you were preparing your report, did you
3	Q. What was the subject matter of	3	review any literature on market
4	that paper?	4	microstructure?
5	A. I don't believe they talked about	5	A. No, not for preparing this report.
6	the motivations of bringing -- I don't believe	6	I -- based on my training and my education,
7	they talked about the motivations for people to	7	I've obviously read a lot of articles on market
8	bring lawsuits alleging market manipulation in	8	microstructure and that forms sort of the
9	that paper. I think it was more of a	9	background or base of my knowledge, but I did
10	descriptive analysis of the types of firms that	10	not specifically review any for this -- for
11	issue future price securities and how most of	11	this engagement.
12	them are extremely small, risky firms.	12	Q. Did you review any literature that
13	Q. Did F -- did FTI recently issue	13	related trading activity to price changes?
14	future price securities?	14	MR. SOHN: Anything?
15	A. I would be very surprised. Well,	15	MR. GUIDO: Any literature.
16	what do you mean by that? Could you define a	16	A. For this engagement?
17	future price security for me?	17	Q. For this engagement.
18	Q. Did it recently issue a	18	A. No, I don't believe I did.
19	convertible debenture?	19	Q. Do you consider yourself an expert
20	A. Well, that's a different -- that's	20	on trading activity and price changes?
21	a different instrument than a future price	21	A. I would consider myself an expert
22	security.	22	in financial economics, financial instruments
23	Q. Okay.	23	and financial markets, and understanding how to
24	A. So, they may have -- they may have	24	measure the stock pricing impact of a news
25	issued a convertible bond. I don't know.	25	announcement or an event or trade. I consider

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	myself an expert in those areas.	2	through impact -- trading impact on the stock.
3	Q. So, prior to this case and Pet	3	There's various theories that have
4	Quarters, had you ever done an analysis of the	4	been tested by and run by people such as
5	relationship between trading activity and price	5	Professors Glosten and Jones.
6	change?	6	Q. What did -- what sort of work did
7	A. Not in terms of my consulting	7	Professor Glosten and Jones do that you just
8	work, no.	8	referred to?
9	Q. Okay. In any other context?	9	A. Various studies they've done.
10	A. It may -- I may well have. I	10	Q. Well, can you name one of them?
11	believe I did do study courses on that for my	11	A. I can -- I can't name the title of
12	Ph.D. training. I reviewed articles and	12	it. It looks at the impact on price of
13	studied articles on that as part of my Ph.D.	13	trading.
14	training in finance and economics.	14	Q. And what -- it looks at the impact
15	Q. When did you get your Ph.D.?	15	of price on trading or trading on price?
16	A. I'm sorry?	16	A. On price of trading.
17	Q. When did you get your Ph.D.?	17	Q. On the price of trading.
18	A. 1989.	18	And what does -- what does it
19	Q. 1989. So that's 20 years ago.	19	measure in terms of the impact on the price of
20	A. Yes. I may also have reviewed	20	trading?
21	literature around that topic for my CFA	21	A. Well, I'd have to look at the
22	charter.	22	article to be -- to be able to tell you. I
23	Q. When did you get your CFA charter?	23	can't sit here and --
24	A. Nine -- 2001, I believe.	24	Q. Did you look at the article before
25	Q. Okay. So that was about nine	25	you --
	Page 19		Page 21
1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	years ago.	2	MR. SOHN: Mr. Guido, you --
3	A. Yes.	3	MR. GUIDO: Excuse me.
4	Q. Did you go back after you were	4	MR. SOHN: He wasn't finished with
5	retained to prepare this report to review the	5	his answer.
6	literature that you had studied in your Ph.D.	6	A. I'd have to look at the article
7	program and when you got your CFA on trading	7	specifically to tell you exactly what they did
8	activity and price changes?	8	and exactly how they measured things.
9	A. I didn't -- I didn't review any	9	Q. Well, did you look at their
10	specific literature. I used my knowledge	10	articles before you wrote that report?
11	gained as an economist for 25 years in	11	A. No.
12	financial economics.	12	Q. What does the -- what do the
13	Q. The -- well, based on your	13	articles that Professor Jones and Professor
14	recollection of what you studied 10 and 20	14	Glosten wrote suggest about the appropriate
15	years ago, can you tell us what theories of	15	measure of active in determining prices?
16	price change in tradings are in the	16	A. Again, I'd have to look at the
17	literature?	17	specific article to be able to tell you.
18	MR. SOHN: Which literature? The	18	Q. Okay.
19	literature that he read 20 years ago?	19	A. I believe one of the things
20	Q. The ones you reviewed 20 years ago	20	they -- they look at is whether there's a trade
21	and 10 years ago.	21	or not.
22	A. Yeah, I mean, there's various	22	Q. Okay. Well, is one of the -- have
23	theories about trading behavior and how it	23	you seen any literature that indicates that --
24	affects the price through inventory	24	with regard to analyzing trading that buys more
25	adjustments, through asymmetric information,	25	prices up and sells more prices down?

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. I'm generally aware that I think</p> <p>3 there are some results that suggest that, yes.</p> <p>4 Q. Okay. And that -- how are buys</p> <p>5 defined in that literature?</p> <p>6 A. I think the literature would</p> <p>7 probably have different definitions of buys,</p> <p>8 depending on who's doing the study. I mean,</p> <p>9 there's lots of studies out there.</p> <p>10 Q. Well, is one of the definitions of</p> <p>11 buys are trades executed at the offer or above</p> <p>12 the offer?</p> <p>13 A. I don't know about -- above maybe.</p> <p>14 Yeah, could be.</p> <p>15 Q. Okay. And that sells are sells if</p> <p>16 the bidder put in a lower bid?</p> <p>17 A. That may be, too.</p> <p>18 Q. In fact, didn't -- didn't you have</p> <p>19 a -- such a study done in Pet Quarters?</p> <p>20 MR. SOHN: Objection.</p> <p>21 A. I'd have to see the Pet Quarters</p> <p>22 report to see exactly what you're referring to.</p> <p>23 We did an initial report and a rebuttal report.</p> <p>24 We did a lot of analysis in there. So I'd like</p> <p>25 to see the report to see exactly what you're</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Well, let me ask you, what is</p> <p>3 your understanding of why transactions move</p> <p>4 prices?</p> <p>5 A. Transactions can move prices for</p> <p>6 information reasons; for supply and demand</p> <p>7 reasons on the inventory of a broker. Reasons</p> <p>8 like that.</p> <p>9 Q. Well, in the papers that you</p> <p>10 studied 20 years ago and 10 years ago, did they</p> <p>11 suggest what the key measures of trading</p> <p>12 activity would be when looking to -- at price</p> <p>13 changes?</p> <p>14 A. I believe they used a variety of</p> <p>15 different trading measures, one of which is</p> <p>16 whether a trade occurred or not.</p> <p>17 Q. Well, can you tell us what</p> <p>18 literature says that?</p> <p>19 A. I think that's in the Glosten and</p> <p>20 Jones papers and other papers.</p> <p>21 Q. What are the other papers?</p> <p>22 A. Well, I can't name them</p> <p>23 specifically for you, but I know there's a body</p> <p>24 of literature out there.</p> <p>25 Q. Does the body of literature</p>
Page 23	Page 25
<p>1 - STEPHEN D. PROWSE -</p> <p>2 referring to.</p> <p>3 Q. Well, in -- in the report --</p> <p>4 A. There were two reports.</p> <p>5 Q. There were two reports.</p> <p>6 A. Yes.</p> <p>7 Q. There was an initial report and</p> <p>8 there was -- there was a rebuttal report.</p> <p>9 A. Yes.</p> <p>10 Q. And was one of the reports -- one</p> <p>11 of the studies that you did, was the impact on</p> <p>12 purchases at the offer on the price of Pet</p> <p>13 Quarters stock?</p> <p>14 A. Sitting here, I'd have -- I can't</p> <p>15 tell you. I'd have to look at the report, look</p> <p>16 at the analysis, to be able to give you a full</p> <p>17 and complete answer to that.</p> <p>18 Whatever it was we did that you're</p> <p>19 talking about, I'm almost certain it was done</p> <p>20 either in response to or in anticipation of</p> <p>21 what the plaintiffs would do in that -- what</p> <p>22 the plaintiff's expert would do in that report.</p> <p>23 And I think we were pretty clear</p> <p>24 that that's why we were doing it. I'm not</p> <p>25 sure.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 indicate which would be the most powerful tests</p> <p>3 to measure the relationship between trading and</p> <p>4 price change?</p> <p>5 A. I can't tell you without looking</p> <p>6 at a specific article.</p> <p>7 Q. Well, when you did your report,</p> <p>8 did you select different ways of determining</p> <p>9 the relationship between trading and price</p> <p>10 changes?</p> <p>11 A. Yes, we did.</p> <p>12 Q. But you didn't go back and look at</p> <p>13 the literature to see what they had to say</p> <p>14 about that?</p> <p>15 A. I did it based on my understanding</p> <p>16 of the appropriate way to conduct an</p> <p>17 investigation about whether an event, whether</p> <p>18 it be a news announcement or a trading, trade,</p> <p>19 occurred and what impact that had on the price.</p> <p>20 Q. Well, but you didn't -- you didn't</p> <p>21 go back and look at the literature to determine</p> <p>22 which one -- which measure or variable would be</p> <p>23 the more powerful variable to consider in</p> <p>24 determining the impact of trading on prices?</p> <p>25 A. I don't think there is a most</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 powerful variable. I think it depends on the</p> <p>3 facts and circumstances of the case, the</p> <p>4 trading, the firm, exchange the firm trades on,</p> <p>5 liquidity of the stock. Lots of things.</p> <p>6 And, so, that's why I think you</p> <p>7 need to look at a variety of different measures</p> <p>8 of potential trading activity.</p> <p>9 Q. Well, if you look at -- let's</p> <p>10 take that and let's look at a couple of</p> <p>11 examples.</p> <p>12 If you're looking at the trading</p> <p>13 to try to determine what impact trading had in</p> <p>14 December of 2009, between December 1st, 2009</p> <p>15 and December 10th, 2009, would it be</p> <p>16 appropriate to look at the trading that</p> <p>17 occurred in January two thousand -- January 1,</p> <p>18 2007 and January 31st of 2007?</p> <p>19 MR. SOHN: Can we -- can you just</p> <p>20 read that back so we can make sure we're all</p> <p>21 together?</p> <p>22 (Whereupon, the record is read</p> <p>23 back.)</p> <p>24 A. It depends on what -- overall what</p> <p>25 big-picture question you're trying to answer.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. Well, that's an incomplete</p> <p>3 hypothetical. What's the question you're</p> <p>4 trying to answer?</p> <p>5 Q. I asked you is it relevant --</p> <p>6 A. Whose trades are you looking at</p> <p>7 and what's the purpose of the analysis?</p> <p>8 Q. Well, the purpose -- I'll give you</p> <p>9 the purpose of the analysis. To determine</p> <p>10 whether or not the trading that occurred by "X"</p> <p>11 in -- between December 1st, 2009 and December</p> <p>12 31st of 2009, and you're trying to determine</p> <p>13 what the impact of that trading was during that</p> <p>14 time period.</p> <p>15 Is the time period of what that</p> <p>16 person did on January 1, 2007 through January</p> <p>17 31st, 2007 relevant?</p> <p>18 MR. SOHN: I'm going to object to</p> <p>19 the form of the question, and it's been asked</p> <p>20 and answered.</p> <p>21 A. Yes, it's relevant. If you're</p> <p>22 trying to determine whether an entity "X" had</p> <p>23 an impact on the price in December, you</p> <p>24 certainly want to look at December. But if "X"</p> <p>25 is also trading in the stock other months, you</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 If you're trying to answer the question that</p> <p>3 we're trying to answer in this case, I think</p> <p>4 you need to look at the -- one of the things</p> <p>5 you need to look at is the entire trading range</p> <p>6 of the defendant, all the dates that he traded,</p> <p>7 to understand what, if any, price impact there</p> <p>8 is as a result of those trades.</p> <p>9 Q. I'm sorry, I didn't ask you about</p> <p>10 this case. I asked you a hypothetical.</p> <p>11 A. And I replied saying it depends,</p> <p>12 and gave you an example of how it might vary.</p> <p>13 And this is a case in how it might be</p> <p>14 important.</p> <p>15 Q. No, you just said that you</p> <p>16 concluded this case is of some importance. I</p> <p>17 think is your answer. Now, the question --</p> <p>18 A. Right.</p> <p>19 Q. Excuse me.</p> <p>20 My question, okay, is is it</p> <p>21 relevant what happened in my hypothetical in</p> <p>22 January 1, 2007 -- between January 1, 2007 and</p> <p>23 January 31st of 2007 in terms of determining</p> <p>24 what the impact of trading was on December 1st,</p> <p>25 2009 through December 31st of 2009?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 want to ask yourself, well, did it have an</p> <p>3 impact in those other months? And if it</p> <p>4 didn't, why am I finding -- why -- that may</p> <p>5 influence how you're looking at December. Or</p> <p>6 if it did, that may also influence on how</p> <p>7 you're looking at December.</p> <p>8 Q. Okay. So that's not -- that's --</p> <p>9 A. So I think if you're looking at an</p> <p>10 entity impact on a stock, entity's trades, you</p> <p>11 need to look at all of their trades.</p> <p>12 Q. Well, when you're looking at --</p> <p>13 you're taking "X," using my hypothetical "X,"</p> <p>14 and we're using the early time period of in '07</p> <p>15 and comparing to the later time period in '09,</p> <p>16 okay, and you indicated that what the person</p> <p>17 did in the earlier time period could be</p> <p>18 relevant to what he did in the later time</p> <p>19 period. Is that fair?</p> <p>20 A. Not only what he did, but what the</p> <p>21 impact was, whether there was an impact on the</p> <p>22 price.</p> <p>23 Q. Now, would it be important to know</p> <p>24 what his motivations were in those two time</p> <p>25 periods?</p>

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 A. It might be, but sometimes you	2 nonparametric tests and the regression
3 don't know that.	3 analysis -- what tests to run and what
4 Q. Okay.	4 specifications to run.
5 A. I mean...	5 Q. Okay. Well, let's take Regression
6 Q. Well, but is motivation an	6 Number 1.
7 important factor to determine whether or not	7 Do you have the report in front of
8 the model you developed is relevant?	8 you?
9 A. It might be.	9 A. Yes.
10 Q. Did you try to determine what the	10 Q. Look at 13B, Exhibit 13B.
11 motivation was here?	11 Do you have that in front of you?
12 A. We weren't asked to determine	12 A. Sorry?
13 intent. We were asked to look at the data to	13 Q. Do you have that in front of
14 understand what the data told us about what the	14 you?
15 price impact was and to objectively look at the	15 A. I didn't say.
16 trading strategy and understand whether that	16 Q. What is -- what -- what is the
17 was a legitimate optimal-type trading strategy	17 variable, the independent variable, for
18 to employ based on the characteristics of	18 Regression Number 1?
19 Sedona and based on the characteristics of the	19 A. There are two independent
20 FPS.	20 variables: One is the NASDAQ return, and one
21 Q. Well, did you attempt to decide --	21 is any Rhino open market trade.
22 to determine what the impact of buys were on	22 Q. What do you mean by "open market
23 prices?	23 trade"?
24 MR. SOHN: You're talking about	24 A. A buy or a -- a trade. A buy or a
25 this case now?	25 sell.
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 MR. GUIDO: This case.	2 Q. A buy or a sell.
3 A. Yes.	3 So any time there was a buy or a
4 Q. Did you measure it against bid-ask	4 sell, you indicate a buy one; and if there
5 prices?	5 wasn't, it was a zero. Is that correct?
6 A. No.	6 A. Right. And that's excluding
7 Q. Did you determine what -- did you	7 direct purchases, conversions, transfers,
8 attempt to determine what the impact of sells	8 things like that.
9 were in this case?	9 Q. Okay. And what about the second
10 A. Yes.	10 regression? What was the independent variable
11 Q. Did you attempt to determine	11 there, or variables?
12 whether the sells were at the ask? I'm sorry,	12 A. Regression Number 2, there were
13 at the bid. Excuse me.	13 three independent variables.
14 A. We looked at the impact of buys	14 Q. Okay.
15 and sells on the stock price.	15 A. The NASDAQ return, Rhino purchases
16 Q. Okay. But you didn't look to see	16 and, thirdly, Rhino sales.
17 whether or not the buys and sells were the bid	17 Q. And those are open market sales
18 or the ask?	18 and purchases?
19 A. I believe we did not.	19 A. Correct.
20 Q. Who selected the variables for the	20 Q. And those are transactions
21 various regressions that were included in the	21 reported to the market?
22 expert report?	22 A. I believe so, yes.
23 A. Tsvetan Beloreshki -- Beloreshki	23 Q. Okay. And the third regression,
24 and I jointly agreed that, for all of our	24 what were the independent variables there?
25 statistical tests -- the parametric tests,	25 A. There were five independent

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	variables.	2	were here?
3	Q. Okay. And what were those?	3	A. The number of shares?
4	A. The NASDAQ return, Rhino	4	Q. The number of shares that were
5	purchases, Rhino sales, transfers between Rhino	5	transferred -- transfers or principals in the
6	accounts, and principal transactions which are	6	data that you looked at.
7	either conversions or direct purchases of stock	7	A. No, not -- not sitting here off
8	from Sedona.	8	the top of my head. I could look at the data
9	Q. And that's -- is that the fourth?	9	and tell you just by adding them up.
10	I mean is that the third? I'm sorry.	10	Q. Well, do you have any charts that
11	A. That's the third regression.	11	indicate whether that -- whether you considered
12	Q. The third regression. Okay.	12	that variable in your report as an exhibit to
13	A. Yes.	13	your report?
14	Q. Now, in that regression, were	14	MR. SOHN: Objection to form.
15	there transfers reported to the market?	15	A. What variable?
16	A. I don't -- I don't believe they	16	Q. The size of the transfers in terms
17	were.	17	of number of shares to the size of the
18	Q. Okay. Well, did you go out and	18	principals compared to the number of shares.
19	attempt to ascertain whether they were reported	19	A. That regression is not reported
20	to the market?	20	here, but I believe that that is one of the
21	A. We didn't determine that. It	21	variables we ran in one of our regressions.
22	wasn't relevant to our analysis.	22	Q. Well, you believe or you reviewed
23	Q. And what about the principal?	23	it before you signed that report?
24	What are those?	24	A. I don't understand your question.
25	A. As I said before, those were	25	Q. Well, I mean, I'm asking you what
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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	either conversions of the FPS into Sedona stock	2	you did. I'm not asking you what you believe.
3	or direct purchases of Sedona stock by Rhino.	3	A. I'm -- I'm saying that we ran a
4	Q. And this is the time period May	4	number of regressions. Four are reported here.
5	1st through May 31st. Is that correct?	5	In one of those other -- these are just flags.
6	A. No.	6	Okay? Zero/ones. So they don't count the
7	Q. Are you looking at 13B or 13A?	7	number of shares.
8	A. I'm looking at 13B.	8	But I believe one of the other
9	Q. What's the time period?	9	regressions that we ran counted the number of
10	A. The time period is March 1st, 2001	10	shares involved in transfers and principal.
11	through May 31st, 2001.	11	Q. No, but did you ever determine
12	Q. During that time period.	12	what the magnitude of the transfers in the
13	Do you know what the -- the number	13	principals were in relationship to the other
14	of transfers in terms of shares and the number	14	transactions that were engaged in by Badian in
15	of principals and conversions of nonmarket	15	this case? You refer to Badian as Rhino.
16	transactions were during that time period?	16	A. We didn't do that specific
17	A. I know there were a number of	17	calculation. That's easily done just by
18	conversions. Four or five at least, probably;	18	looking at the data.
19	maybe more. There may have been a direct	19	Q. You didn't do that, did you?
20	purchase of stock in there, as well. I don't	20	A. We didn't do the specific
21	know off the top of my head.	21	calculation, but it basically is inherent in
22	And I couldn't tell you without	22	the data.
23	looking at the data how many transfers were in	23	Q. Well, I mean -- I mean, is it
24	that period.	24	relevant what the size is in terms of the
25	Q. So you don't know what the numbers	25	total number of transactions that you're

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	considering --	2	A. -- that other investors might
3	MR. SOHN: Objection to form.	3	obtain by virtue of knowing that a
4	Q. -- whether it's principal and	4	conversion happened --
5	transfers as opposed to open market sales?	5	Q. Do you --
6	A. Well, if it's relevant, it will	6	MR. SOHN: Mr. Guido.
7	show up in the regression results in terms of	7	MR. GUIDO: I'm sorry.
8	having a price impact.	8	A. -- or a direct purchase happened.
9	Q. Or not having one.	9	Q. So you included in your analysis
10	A. Exactly. And that will tell you	10	conversions and transfers, although you didn't
11	whether it's relevant or not.	11	know whether or not they were -- that
12	Q. Well, if a transaction is not	12	information was available to the market at the
13	reported to the market, how does that have a	13	time?
14	price impact?	14	A. We didn't do a study to determine
15	A. There -- it could easily have a	15	that, but that's a complete and legitimate
16	price impact. Just the information that	16	channel through which price might be affected.
17	someone has converted is important information	17	And, so, we wanted to test that.
18	for investors in that firm. That's a big	18	Q. Well, what's -- what has to happen
19	event. That means that the person that's	19	before it has an impact?
20	converted has a large number of shares, which	20	A. I've already told you.
21	if he hasn't -- if he hasn't shorted them	21	Q. It's available to the market.
22	earlier, that's important information that an	22	Right?
23	investor might like to know.	23	A. The information -- if the
24	And, so it's quite, quite	24	information of a conversion or a direct
25	legitimate to test to see whether a non -- an	25	purchase becomes available to the market.
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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	off-market transaction might have an impact on	2	that's important information. It's documented
3	the stock through that information.	3	in the economic literature that issuance of
4	Q. Well, did you -- did you try and	4	stock is important information to investors.
5	determine whether or not that information was	5	And if other investors become aware of it, then
6	available to the market? Conversions.	6	that's important information that may have an
7	A. We didn't -- we didn't determine	7	impact on the price.
8	whether the information was available to the	8	Q. Now, I think there's one more
9	market or not. We tested in our regression	9	regression that's reported here?
10	whether that channel of information might have	10	A. There's Regression Number 4 in
11	had an impact.	11	Exhibit 13B.
12	Q. Okay. But you don't know whether	12	Q. Okay. And what were the variables
13	or not it was reported to the market?	13	that were included there?
14	A. I don't know. I don't know	14	A. There were two independent
15	whether the market became aware of the	15	variables: The NASDAQ return, and net daily
16	conversion soon after it happened.	16	shares transacted as a percent of total
17	Q. Okay.	17	reported trading volume.
18	A. But --	18	Q. So there were three: NASDAQ, net
19	Q. But is it important for the market	19	transactions, and the market volume. Is that
20	to be aware of the transaction to measure it as	20	right?
21	having an impact on price of Sedona stock?	21	A. No, there are two independent
22	A. Well, that's the channel through	22	variables. There are three pieces of
23	which the price might be impacted, is the	23	information that go into those variables.
24	information that other --	24	Q. Okay.
25	Q. You didn't --	25	A. One is the NASDAQ return; and the

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1 - STEPHEN D. PROWSE - 2 other two, which go into one variable, are net 3 daily shares transacted as a percent of total 4 reported trading volume. 5 Q. Okay. And -- and -- what -- what 6 went into determining the net transactions? 7 A. Net daily shares transacted was 8 just the net -- the net of buys and sells. 9 Q. Buys and sells or buys, sells, 10 transfers and -- 11 A. Buys and sells. 12 Q. Just buys and sells? 13 A. Buys and sells. 14 Q. Not transfers and not principal -- 15 A. Not transfers, not principal. We 16 ran another regression that included those. 17 Q. Now, which one of the two is 18 included in Exhibit 13B? 19 A. Regression number 4 is -- one of 20 the independent variables in Regression Number 21 4, the numerator of that variable is net daily 22 shares transacted. Net daily shares transacted 23 is computed as buys minus sells as I previously 24 defined buys and sells. 25 Q. I'd like you to take a look at a	1 - STEPHEN D. PROWSE - 2 if I give the witness this version? It's a 3 little better. Maybe he could see it easier. 4 MR. GUIDO: That's fine. 5 MR. SOHN: Okay. 6 MR. GUIDO: I'm sorry, but the 7 court reporter condensed it. 8 MR. SOHN: Yeah. 9 A. Yeah, I think I'm -- I think I'm 10 there. 11 Q. Okay. 12 A. Well, there are a large number of 13 sheets with AS -- columns AS through A -- 14 Q. Yeah, I mean, but -- but I'm -- 15 what I want you to look at is the first -- or 16 the first of the sheets that have AS through 17 AW, because it has the calculations at the top 18 of it, of this sheet. 19 A. Okay. I think I'm there. 20 Q. Now, it has -- in AS it says 21 "Regression 4," and in AV it says "Regression 22 5A." 23 Do you see that? 24 A. No. 25 Q. I mean 4A. Excuse me.
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1 - STEPHEN D. PROWSE - 2 document that has been marked as Exhibit No. 3 14. 4 MR. SCHECHTMAN: I'm sorry, what 5 number did you say? 6 MR. GUIDO: Fourteen. 7 MR. SCHECHTMAN: Fourteen? 8 MR. GUIDO: Yes, Deposition 9 Exhibit No. 14. I had put a Tab 13B on it from 10 BP-04. And as I explained to Mr. Sohn 11 yesterday, that if you look at B-4, this is 12 really, I think, something called SDA -- SDAN. 13 It is not 13B, but it's the backup for Exhibit 14 13B. 15 BY MR. GUIDO: 16 Q. I want to direct your attention. 17 Does that have -- at the top -- across the top 18 there are columns, I think. Is that correct? 19 It starts, I think, with "B" and then it moves 20 on -- 21 A. Yes. 22 Q. I'd particularly like to address 23 your attention to the second set which is -- I 24 think it's AU -- or it's AS through AW. 25 MR. SOHN: Mr. Guido, do you mind	1 - STEPHEN D. PROWSE - 2 A. I see that. 3 Q. Okay. Now one of them says -- AT, 4 it says "Net daily sales transacted as A 5 percentage of volume." AT it says. 6 In AW it says "Net trading as 7 percentage of volume." Although your Exhibit 8 13B in your report says, "Net daily shares 9 transacted as a percent of the total reported 10 trading volume." 11 Which is which? 12 A. I believe the results that are 13 reported in Regression 4 are the results 14 associated with the Regression 4A, net trading 15 as a percent of volume. 16 Q. Okay. And what's the "P" value 17 there? 18 A. Seven percent. 7.08 percent. 19 Q. All right. And what percentage of 20 significance is that? 21 MR. SOHN: Objection to form. 22 A. I don't understand your question. 23 Q. Well, is it -- is it -- is it 92.9 24 here? 25 A. It's not significant --

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 significant at the 95 percent level, which is</p> <p>3 the level we used here.</p> <p>4 Q. But it is significant at the 90</p> <p>5 percent level if you use the 90 percent</p> <p>6 level?</p> <p>7 A. If you use the 90 percent level,</p> <p>8 yes, it is.</p> <p>9 Q. Okay. Have you used the 90</p> <p>10 percent level?</p> <p>11 A. I haven't used the 90 percent</p> <p>12 level. I've used the 95 percent level.</p> <p>13 Q. Did you use the 90 in Pet</p> <p>14 Quarters?</p> <p>15 A. I don't believe we used 90 in Pet</p> <p>16 Quarters for the variables of interest. We may</p> <p>17 have -- we may have talked about something</p> <p>18 being weakly significant at 90.</p> <p>19 Q. But you did talk about 90 percent</p> <p>20 significance level?</p> <p>21 A. You'd have to show me the Pet</p> <p>22 Quarters report.</p> <p>23 Q. Well, I'm just asking you what you</p> <p>24 know.</p> <p>25 A. And without looking at the report,</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. I believe -- let me turn to</p> <p>3 Exhibit 3. The way it's written here, we don't</p> <p>4 have a -- we don't have a journal associated</p> <p>5 with it, but I do believe it came out in a</p> <p>6 peer-reviewed journal. We may have been</p> <p>7 referring here to the working paper, but I do</p> <p>8 believe it did come out in a peer-reviewed</p> <p>9 journal.</p> <p>10 Q. What's the significance of</p> <p>11 something being in a peer-reviewed journal?</p> <p>12 A. It means it's been reviewed by --</p> <p>13 it's gone through a peer-review process.</p> <p>14 Q. What's the significance of that?</p> <p>15 A. It means it's gone -- gone through</p> <p>16 a peer-review process and it's been approved</p> <p>17 for publication because it's relevant and of</p> <p>18 interest to -- the editor thinks it's of</p> <p>19 relevance and of interest to the readers of the</p> <p>20 journal.</p> <p>21 Q. You've written peer-reviewed</p> <p>22 articles, haven't you?</p> <p>23 A. Yes.</p> <p>24 Q. And, in fact, you claim that it's</p> <p>25 a positive for your qualifications as an expert</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 I couldn't give you the specifics apart from</p> <p>3 what I've already given you.</p> <p>4 Q. You remember or you don't. Okay.</p> <p>5 Now, the -- this Exhibit 13B, from</p> <p>6 your testimony, you said it's not significant</p> <p>7 at the 95 percent level, but the</p> <p>8 significance -- if you use your calculations,</p> <p>9 the significance is 92.92 percent, is it not?</p> <p>10 MR. SOHN: Objection to the form.</p> <p>11 A. On a stand-alone basis, correct,</p> <p>12 but none of these regressions are significant</p> <p>13 after you apply the appropriate correction to</p> <p>14 them.</p> <p>15 Q. Well, we'll talk about that a</p> <p>16 little later.</p> <p>17 The -- now, I want to go back to</p> <p>18 the literature that you were aware of with</p> <p>19 regard to how the market performed.</p> <p>20 And I think you mentioned the</p> <p>21 market conditions. Excuse me. I think you --</p> <p>22 you mentioned one study that was -- that you</p> <p>23 reviewed. That's the Chaplinsky piece.</p> <p>24 Was that in a peer-reviewed</p> <p>25 journal?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 witness, do you not?</p> <p>3 A. I don't think I claim it as a</p> <p>4 positive. It's the truth, so I put it down.</p> <p>5 Q. Okay. Well, how tall are you?</p> <p>6 A. Six-three and three-quarters.</p> <p>7 Q. Okay. Do you put that down?</p> <p>8 A. No.</p> <p>9 Q. Okay. So you thought it was</p> <p>10 relevant that you put it -- that you published</p> <p>11 articles in peer-reviewed journals, didn't</p> <p>12 you?</p> <p>13 A. I did think it was relevant.</p> <p>14 Q. And the question is why you</p> <p>15 thought it was relevant.</p> <p>16 A. Because people would be interested</p> <p>17 to know that I've published in peer-reviewed</p> <p>18 journals.</p> <p>19 Q. And what's the significance of</p> <p>20 publishing in a peer-reviewed journal?</p> <p>21 MR. SOHN: Objection.</p> <p>22 A. That you have had articles</p> <p>23 published on relevant topics in peer-reviewed</p> <p>24 journals.</p> <p>25 Q. Okay. And -- and having an</p>

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 article published in a peer-reviewed journal as</p> <p>3 opposed to nonpeer-reviewed journals indicates</p> <p>4 that it's more accepted in the scientific</p> <p>5 community?</p> <p>6 MR. SOHN: Objection to form.</p> <p>7 A. I believe -- I wouldn't agree with</p> <p>8 that the way you stated it. I mean, there are</p> <p>9 plenty of articles out there that are -- that</p> <p>10 may not have appeared in peer-reviewed</p> <p>11 journals, but are used. But generally going</p> <p>12 through a peer review process shows that your</p> <p>13 article has been deemed relevant and</p> <p>14 interesting.</p> <p>15 Q. And significant?</p> <p>16 A. Well, I don't know about</p> <p>17 significant. Relevant and interesting.</p> <p>18 Q. Okay. Now, have you published</p> <p>19 anything in any journals on micro -- market</p> <p>20 microstructure studies?</p> <p>21 A. I don't believe you would call any</p> <p>22 of the peer-reviewed analysis I've done,</p> <p>23 studies I've done, under the heading of market</p> <p>24 microstructure. I think we categorize them</p> <p>25 under the heading of how financial markets</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Excuse me. That's the next one</p> <p>3 above?</p> <p>4 A. That's the next one above.</p> <p>5 Q. Okay.</p> <p>6 A. Then, the next one above that, "An</p> <p>7 Economic Analysis of the Private Equity</p> <p>8 Market."</p> <p>9 Q. Okay.</p> <p>10 A. And then, the next one above that,</p> <p>11 "Innovation and Finance in High-Tech Firms."</p> <p>12 Q. Okay.</p> <p>13 A. Then, the next one above that,</p> <p>14 "Angel investors and the Market for Angel</p> <p>15 Investments."</p> <p>16 Those would all be articles that</p> <p>17 either touch on or focus specifically on the</p> <p>18 financial markets that are available to small,</p> <p>19 risky firms.</p> <p>20 Q. Okay. Do any of those --</p> <p>21 A. So there -- hang on. I'm not</p> <p>22 done. There are others.</p> <p>23 Q. I'm sorry.</p> <p>24 A. That topic may be touched on in</p> <p>25 the two articles at the bottom of the first</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 work, how financial instruments work. In</p> <p>3 particular, how financial markets work for</p> <p>4 small, risky firms like Sedona. I think that</p> <p>5 would be the cate -- category that I would</p> <p>6 place them under.</p> <p>7 Q. Well --</p> <p>8 A. Among other categories.</p> <p>9 Q. Well, take a look at your resume.</p> <p>10 Can you point out which one of those you're</p> <p>11 referring to?</p> <p>12 A. Well, there are a variety of</p> <p>13 articles that touch on or focus on how firms</p> <p>14 raise finance. In particular, how small, risky</p> <p>15 firms raise finance. Those would be the</p> <p>16 following: "Recent Developments in Corporate</p> <p>17 Finance," the last one on the list.</p> <p>18 Q. What was --</p> <p>19 A. The last one -- the last one on</p> <p>20 the list. I'm starting at -- I'm going -- I'm</p> <p>21 starting at the latest and moving forward.</p> <p>22 Q. Okay.</p> <p>23 A. The -- "A Look at America's</p> <p>24 Corporate Finance Markets; "The Economics of</p> <p>25 the Private Placement Market: A New Look."</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 page of Exhibit 1, "Corporate Finance and</p> <p>3 Governance in an International Perspective."</p> <p>4 And "Corporate Governance in Eastern Europe and</p> <p>5 Russia: The Role of Banks." May be touched on</p> <p>6 in "Alternative Models of Financial System</p> <p>7 Development," the one above that.</p> <p>8 There's two art -- three</p> <p>9 articles --</p> <p>10 Q. Excuse me, I'm sorry. I missed</p> <p>11 that last one. What was it?</p> <p>12 A. "Alternative Models of Financial</p> <p>13 System Development." It's third from the</p> <p>14 bottom.</p> <p>15 Q. Okay.</p> <p>16 A. Eight from the bottom, "Trends and</p> <p>17 Prospects in Venture and Angel Investments in</p> <p>18 New Media Companies."</p> <p>19 Q. Okay.</p> <p>20 A. The one above that, "Angel</p> <p>21 Investors and the Angel Capital Electronic</p> <p>22 Network."</p> <p>23 The one above that, "The Private</p> <p>24 Equity Market."</p> <p>25 And, again, those are all articles</p>

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	that focus on the financial -- how the financial	2	relative merits of different forms of
3	markets for small, risky firms behave; what the	3	financing?
4	incentives are for providers of finance and	4	A. Well, we take -- we look at it
5	users of finance and how contracts are	5	from the point of view of economics, which --
6	structured. Financial contracts are structured	6	from a positive viewpoint as opposed to a
7	between the providers of finance and firms with	7	normative viewpoint. We look at costs and
8	regards to the types of securities that those	8	benefits of different types of financing
9	small, risky firms will use.	9	instruments. And we can -- we either imply or
10	Then there is another article,	10	conclude that, you know, certain ways of
11	"Dura's Impact on Damages," which doesn't talk	11	raising finance for small, risky firms are just
12	about that -- that topic talks about event	12	not possible because of the costs involved.
13	studies.	13	The asymmetric -- asymmetric information costs,
14	Q. I think that what you just said is	14	corporate control costs, other costs. Things
15	that these articles addressed how financial	15	like that.
16	instruments are structured to raise capital for	16	And, therefore, they are forced to
17	companies.	17	go to other forms of finance such as the
18	Is that a fair characterization?	18	private equity market and the private debt
19	A. No.	19	market.
20	Q. Okay.	20	Q. Okay. But the thrust of the --
21	A. They either touch on or focus on	21	the thesis here is the benefits and cost of
22	how small firms that don't have access to, say,	22	either going to the corporate bond market and
23	the corporate bond market or even the corporate	23	the issuance of on-the-spot stock as opposed to
24	equity market, how they raise finance. And the	24	privately negotiated instruments?
25	various different players in -- in the	25	A. I wouldn't say that's the focus.
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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	financial markets that they do have access to,	2	I'd say that was -- that's part of what was --
3	such as the private equity markets, such as the	3	I'd say the focus is on how exactly are the
4	private placement market.	4	private equity markets and the private debt
5	And the roles and incentives of	5	markets structured? What types of financial
6	the providers of finance and the -- the lenders	6	instruments do we see existing in those markets
7	and the users of finance, the firms, to -- how	7	and why do we see them?
8	their -- how their incentives interplay to come	8	Q. Okay. Did you --
9	up with the characteristics of the financial	9	A. And that's based on the costs and
10	instruments that are actually used for the	10	benefits to the investors and the firms of
11	small firms to raise finance.	11	entering into financial contracts with each
12	Q. Do any of these articles address	12	other.
13	the benefits and costs to the -- the investors?	13	(Cell phone ringing.)
14	A. Absolutely. They talk a lot about	14	MR. GUIDO: Excuse me.
15	the structures that investors put in place to	15	We have to go off the record.
16	ensure that their -- they get a return on their	16	Cellular phone.
17	money.	17	THE VIDEOGRAPHER: Going off the
18	Q. Do any of these address the	18	record at 11:10 a.m.
19	benefits to the users for the issuance of these	19	(A recess is taken.)
20	instruments?	20	THE VIDEOGRAPHER: Going back on
21	A. Absolutely. They talk about the	21	the record at 11:21 a.m.
22	benefits to the users of structuring contracts	22	BY MR. GUIDO:
23	in particular ways in order to raise finance of	23	Q. When we broke, I was asking you
24	most favorable terms.	24	about your publications. And one of the
25	Q. Do any of these address the	25	questions I have for you is, do any of those

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 address the risks and benefits of future price</p> <p>3 securities to the issuer?</p> <p>4 A. Most of this work was done in the</p> <p>5 early '90s, before future price securities came</p> <p>6 on the scene, basically.</p> <p>7 Q. Okay.</p> <p>8 A. I think the studies tell us that</p> <p>9 the first future price securities were out</p> <p>10 there around 19 -- 1995. And while that was</p> <p>11 still a specialty of mine, small firm finance</p> <p>12 and how firms raise finance, I was very aware</p> <p>13 of future price securities around that time</p> <p>14 period, I don't believe a discussion of those</p> <p>15 got into any of these articles, with the one</p> <p>16 exception of the private equity market in the</p> <p>17 Handbook of Corporate Finance in 2002. I don't</p> <p>18 believe there's a discussion of FPS securities</p> <p>19 in there, but it's possible that there's a</p> <p>20 reference to them.</p> <p>21 But most of my articles were</p> <p>22 written in the early '90s, and the focus was on</p> <p>23 securities, you know, similar to FPS securities</p> <p>24 and the role they played in terms of giving</p> <p>25 firms access to finance that didn't have access</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 the concern was, well, where -- where do they</p> <p>3 go? Where do they go for finance?</p> <p>4 So there was an institutional</p> <p>5 motivation for me to be doing such research,</p> <p>6 but that was a research interest in and of</p> <p>7 itself by me.</p> <p>8 And, so, me and a group of others</p> <p>9 conducted an immense amount of research in that</p> <p>10 time period into the exact issues that, for</p> <p>11 example, Sedona would face in raising finance:</p> <p>12 Where do they go? How do they get it? What</p> <p>13 kinds of contracts could they construct with</p> <p>14 potential investors?</p> <p>15 And, so, there was -- and, so,</p> <p>16 there was definitely a -- a policy-oriented</p> <p>17 motivation, but there was also, just from a</p> <p>18 pure economics motivation, a desire to</p> <p>19 understand how do these markets work that we</p> <p>20 don't know much about that provide finance to</p> <p>21 small, risky firms like Sedona?</p> <p>22 Q. Okay. Thank you.</p> <p>23 Now, in any of these articles, did</p> <p>24 you address the question of market manipulation</p> <p>25 in future price securities?</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 to other forms of finance, but didn't -- didn't</p> <p>3 specifically address FPS securities.</p> <p>4 Q. Well, I mean, a number of the</p> <p>5 papers, I think, that you indicated that you</p> <p>6 had written during that time period seem to</p> <p>7 have been written by -- at the time that you</p> <p>8 were at the Federal Reserve?</p> <p>9 A. Yes.</p> <p>10 Q. And were those papers that were</p> <p>11 intended to educate people on the various forms</p> <p>12 of financing that might be available to assist</p> <p>13 in economic development?</p> <p>14 A. That was part of it. The Fed is</p> <p>15 always interested in research on how firms</p> <p>16 raise finance, particularly those firms that</p> <p>17 don't have access to traditional forms of</p> <p>18 finance, like the corporate bond market and the</p> <p>19 corporate equity market.</p> <p>20 And particularly at this time</p> <p>21 period, we're in the credit crunch. And there</p> <p>22 was a very -- there was a very policy-oriented</p> <p>23 concern that, because of the credit crunch,</p> <p>24 firms -- small, risky firms, like Sedona, were</p> <p>25 getting shut out of traditional markets. And</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. I don't believe we did.</p> <p>3 Q. Now, most of these articles are</p> <p>4 dated, it looks like, prior to 2000.</p> <p>5 A. Most of them. There's one in 2002</p> <p>6 and one in 2001.</p> <p>7 Q. Right.</p> <p>8 A. And one in 2000.</p> <p>9 Q. And there's one in 2008. Let's</p> <p>10 look at the one in 2008.</p> <p>11 Does that address the application</p> <p>12 of an event study to determine what damages are</p> <p>13 in a securities matter?</p> <p>14 A. Yes, specifically in a 10b-5</p> <p>15 matter.</p> <p>16 Q. Okay. And it's an allegation of</p> <p>17 fraud that you're --</p> <p>18 A. It's a.</p> <p>19 Q. -- talking about measuring in that</p> <p>20 article?</p> <p>21 A. An allegation that the firm made</p> <p>22 misrepresentations and omissions that investors</p> <p>23 would have found material.</p> <p>24 Q. And was that in a securities</p> <p>25 filing with the SEC?</p>

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 A. Was what in a security --	2 background market was that might have an effect
3 Q. What you were writing about.	3 on the particular stock price in your study.
4 A. Well, we weren't writing about	4 Is that one of the factors?
5 anything specific to the SEC. We were writing	5 A. That's one of the things that you
6 about what the proper method is to -- in using	6 look at to see how influential market and
7 an event study to analyze the effect of a	7 industry factors are on stock price movements
8 particular news -- a particular event such as a	8 of the company you're interested in.
9 disclosure by a firm.	9 Q. Okay. And you said that you would
10 Q. Well, what were the proper methods	10 focus on the particular event.
11 that you discussed in that paper to do event	11 What did you refer to when you
12 studies?	12 said that?
13 A. Well, event study methodology is	13 A. The particular event you're
14 generally accepted in the economics literature	14 interested in in determining the price impact
15 and finance literature. And there's general	15 of. Whether it be a disclosure, whether it be
16 accept -- I think there's general acceptance	16 some other event. That's what you want to look
17 about how to go about doing an event study.	17 at.
18 There are, obviously, details about an event	18 Q. Is it important that you pick the
19 study that people may disagree about, but I	19 correct event to determine what the impact that
20 think the overall approach to doing an event	20 event had on stock price?
21 study is generally accepted.	21 A. Well, if you know the event, I'm
22 And we talked about that. And	22 not sure there's an issue about picking the
23 then, also, how the legal -- the legal	23 event. If you know the event that you're
24 environment affected -- or the changing legal	24 interested in studying, I'm not sure there's an
25 environment affected the exact method by which	25 issue about picking it. It's kind of a
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 you calculate damages in a shareholder class	2 tautology. Once you determine what the event
3 action using an event study, but also using	3 is, then you measure the impact of it.
4 other methods to calculate damages.	4 Q. Let me ask you, you used the term
5 Q. Well, what were the generally	5 "market manipulation" in this report?
6 accepted methods that you addressed in that	6 A. Yes.
7 article that should be applied in the event	7 Q. What do you mean by that?
8 study?	8 A. Well, I know there are legal
9 A. We talked -- I think -- without	9 definitions of market manipulation. And I'm
10 having the article in front of me, I can't	10 not a lawyer. So I'm not -- I don't want to
11 recall the exact details of what we talked	11 get -- I'm talking from an economics point of
12 about, but we talked about the fact that an	12 view, an economist's point of view. And I
13 event study is a generally accepted way to go	13 understand that one of the -- one of the
14 about doing things.	14 aspects that you look at from an economics
15 And I think we talked in general	15 point of view in -- in determining overall
16 about how you go about doing an event study:	16 whether or not there's been manipulation is
17 You set up a market model; look at daily	17 whether there's been a price impact of the
18 changes in stock returns; understand how stock	18 trades or other -- other transactions.
19 returns vary with various market or industry	19 So I understand that's one element
20 indexes; and then, focus on the particular	20 in the ultimate legal judgment about whether
21 disclosures or events that you're interested in	21 there's been market manipulation or not.
22 focusing on to identify whether there was a	22 Q. No, I'm asking you how you used
23 stock price impact due to those events.	23 the term "market manipulation." It appears
24 Q. So, in other words, in the market,	24 that -- in the very last paragraph of your
25 you'd look to see -- you consider what the	25 expert report.

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 How are you using that term?	2 point in time Badian's trading hit the bid in
3 A. In my last paragraph?	3 the trading.
4 Q. Uh-huh. The one that -- the	4 You also testified that you didn't
5 conclusion paragraph.	5 look to see whether or not Badian's purchases
6 A. Oh, that's the second to last	6 were at the offer.
7 paragraph.	7 How can you determine whether or
8 Q. I'm sorry.	8 not something's a legitimate strategy unless
9 A. Right. The conclusion there comes	9 you look to those two factors?
10 from the analysis we have performed in the	10 MR. SOHN: Objection to form.
11 report, which shows a number of things: One,	11 A. I'm talking about the strategy
12 that Rhino pursued a legitimate strategy in	12 that Rhino employed, because Sedona was an
13 trading Sedona stock given the riskiness of	13 extremely risky company and the FPS was an
14 Sedona and giving the riskiness of the FPS	14 extremely risky security, to short his position
15 security that it was holding.	15 prior to conversion. That isn't -- on a broad
16 Two, that Sedona was an extremely	16 level, overall level, that's an optimal
17 risky company. Sedona knew it; investors knew	17 strategy to pursue.
18 it. And, so, investors had to react and hedge	18 Q. Okay. Let's take that --
19 appropriately.	19 A. Because it -- because it minimizes
20 And, also, the poor performance of	20 your risks. And there are a lot of risks that
21 Sedona shares over any time period can -- can	21 you have to minimize.
22 be contrib -- can be explained by a lot of	22 Q. Okay. Is it -- is it legitimate
23 other fact -- a lot of factors that don't have	23 activity to violate a contract provision?
24 anything to do with manipulation, such as the	24 A. That -- my understanding is that's
25 decline of the overall market, Sedona's	25 not part of the SEC's -- that a violation, any
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 specific -- the decline in Sedona's industry,	2 violation of a contract is not part of the
3 Sedona's peers, and Sedona-specific factors,	3 SEC's allegation, and we weren't asked to look
4 such as, you know, it being a going concern, it	4 at that.
5 never making any money. That type of thing.	5 Q. No, I didn't ask you that
6 And then, finally, the economic or	6 question. I asked you the question whether
7 econometric and statistical analysis which	7 violating a contract provision was a legitimate
8 fails to show any price impact of any kind --	8 strategy.
9 any kind of Rhino trading over any time period	9 MR. SOHN: Objection to form.
10 at all.	10 A. We weren't -- is that a
11 Q. Okay. So, one of -- I mean, one	11 hypothetical?
12 component of your definition of market	12 Q. Yeah.
13 manipulation is that the econometrics failed to	13 A. What do you mean by "legitimate"?
14 show a price impact?	14 Q. I said, does violation of a
15 A. That's one component.	15 contract provision constitute legitimate
16 Q. Okay.	16 activity to you?
17 A. That's one component in our	17 MR. SOHN: Any contract provision?
18 conclusion in paragraph 62.	18 MR. GUIDO: Any.
19 Q. And that the other components was	19 A. What do you mean by "legitimate"?
20 that there was a -- there was a legitimate	20 Q. That -- you're the one who used
21 strategy --	21 the term. What do you mean by it?
22 A. Correct.	22 A. So are you using -- are you asking
23 Q. -- that -- that was used here.	23 -- you --
24 Now, I think you said that you did	24 Q. I'm asking you.
25 not look to see whether or not at any given	25 A. It's your hypothetical, though.

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1 - STEPHEN D. PROWSE - 2 So I just want to make sure that -- 3 Q. My hypothetical is using your term 4 "legitimate." 5 A. Okay. 6 Q. I'm asking whether or not within 7 your term "legitimate" includes violations of 8 contract terms. 9 MR. SOHN: Any contract terms? 10 MR. GUIDO: Any contract terms. 11 A. It may be if there's a dispute 12 over a contract and what a term means. One 13 firm -- one side may say you violated a 14 particular term. The other side may say, no, 15 we interpreted it this way. So there may be -- 16 there may be a dispute. 17 So it may be legit -- perfectly 18 legitimate from one firm's point of view if 19 they don't believe the contract provision means 20 what the other firm says it means. 21 Q. Take the hypothetical that there's 22 no question what the contract term means. 23 Is it legitimate to violate the 24 contract terms using your definition of 25 legitimate?	1 - STEPHEN D. PROWSE - 2 There may be disputes about issues like that. 3 So, you know, I can't answer your 4 hypothetical. 5 Q. Well, assume that there is no 6 dispute about the prohibition against shorting. 7 It's perfectly clear. There is no dispute 8 between the holder of the convertible debenture 9 and the issuer. They don't have a dispute 10 about it. Assume that. 11 Is a violation of that legit -- 12 that provision a legitimate activity in your 13 view, using your term "legitimate activity"?
	14 MR. SOHN: Economic legitimate 15 activity. 16 MR. GUIDO: Just his term 17 "legitimate activity." You're the one who 18 added "economic." The witness said legitimate 19 activity. 20 A. Well, I said before, I'm not -- 21 I'm not a lawyer. So I'm not looking at, for 22 example, market manipulation terms in -- market 23 manipulation in legal terms. 24 So I'm going to answer your 25 question as an economist.
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1 - STEPHEN D. PROWSE - 2 MR. SOHN: So any unambiguous 3 contract terms? 4 MR. GUIDO: Any unambiguous 5 contract terms. 6 A. Well, it's hard for me -- in this 7 world it's hard for me to think of something 8 that's completely unambiguous to anybody, but 9 in your hypothetical it may be. It may be. 10 Q. Well, let me give you another 11 hypothetical, and we'll get closer to this 12 case. You have a contract provision that says 13 you may not short stock prior to submission of 14 a conversion letter. And the person holding 15 the convertible debenture shorts the stock 16 prior to submitting the conversion letter. 17 Is that legitimate activity in 18 your view? 19 MR. SOHN: Legitimate economic 20 activity? 21 MR. GUIDO: Yeah. 22 A. In your hypothetical, again, there 23 may be a dispute about the definition of 24 shorting. There may be a dispute about the 25 meaning of what was meant in the contract.	1 - STEPHEN D. PROWSE - 2 Q. Okay. That's fine. 3 A. And there may be economic reasons 4 that are legitimate to violate a contract. 5 Q. Okay. 6 A. Violate a provision. 7 Q. Are there legitimate economic 8 terms (sic) to rob a bank? 9 A. Legitimate -- 10 MR. SOHN: Objection. 11 A. -- economic reasons? 12 Q. To rob a bank. 13 A. I doubt it because the risks are 14 just too high. 15 Q. Oh, because of the question of the 16 risks? 17 A. Yeah, because the risks are too 18 high of getting caught. 19 Q. So legitimacy in your view is 20 determined by what the risks are? 21 A. From an econo -- I'm saying from 22 an economic -- I'm not answering any of your 23 hypotheticals from a legal perspective. Okay? 24 I don't know what the law is regarding, in your 25 hypothetical, the violation of a particular

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1 - STEPHEN D. PROWSE - 2 provision. 3 From a -- from a purely economic 4 point of view -- and all economists will agree 5 with this. From a purely economic point of 6 view, you weigh the costs and benefits of doing 7 something. And if the benefits outweigh the 8 costs, then you do it. 9 Now, that is from a purely 10 economic point of view. It's taking law out of 11 it, although law might have a role in forming 12 the costs and benefits, and it's taking 13 morality out of it. So it's purely from an 14 economic point of view, weigh the costs and 15 benefits. And you say, how do I -- do I 16 benefit? 17 Q. So the cost and benefit is -- the 18 benefit is whatever the financial benefit is 19 and the cost is getting caught? 20 A. And the cost is whatever the 21 financial cost is. 22 Q. Including getting caught? 23 A. Including the risk of getting 24 caught maybe. 25 Q. And including getting put in jail?	1 - STEPHEN D. PROWSE - 2 law. 3 Q. Well -- 4 A. It recognizes the law. 5 Q. But you said you're not -- you're 6 not using the term "legitimate" in a legal 7 sense. 8 A. Except in your hypothetical when 9 you told me you'd go to -- when you rob a bank, 10 you go to jail. 11 Q. Now, the other point that you make 12 is that you looked at what their performance 13 was over time. 14 A. Yes. 15 Q. And that that affected your view 16 of whether the market was manipulated. 17 What was the time frame that you 18 were comparing? 19 A. We looked -- generally we looked 20 at two different time periods. We looked over 21 the entire time period of Rhino's trading, and 22 we looked at the period March 1st through May 23 31st, 2001. 24 Q. And you looked to see whether or 25 not the price declined over that time period?
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1 - STEPHEN D. PROWSE - 2 MR. SOHN: Objection. 3 A. Well, I'm not sure you get put in 4 jail for violating the provision of a 5 contract. 6 Q. No, but you do get put in jail for 7 robbing a bank, don't you? 8 A. If you get caught, I guess, yeah. 9 Q. I mean -- and that's why I gave 10 you the hypothetical. In terms of -- I'm 11 trying to understand how you're using the term 12 "legitimate activity." 13 So if -- so if -- I gather you're 14 saying is, is that irrespective of what the 15 contract provisions are or legal provisions 16 are, legitimate activity, in economic terms, 17 the way you're using it, is whether or not the 18 benefits outweigh the cost? 19 MR. SOHN: Objection to the form. 20 A. No, that's not true, because the 21 law has an element in forming what the costs 22 are. 23 Q. No, I understand that, but -- 24 A. So you said irrespective of 25 the law. Well, it's not irrespective of the	1 - STEPHEN D. PROWSE - 2 A. We looked to see what happened to 3 the price and what happened to other factors 4 that potentially could have affected that 5 price, such as the market, such as the 6 industry, such as Sedona-specific price -- 7 Sedona-specific events. 8 Q. Well, what events did you look 9 to? 10 A. Well, I can point some out in our 11 section on that. We looked at Section A. We 12 looked at market and industry peer group 13 factors. Section B we looked at Sedona -- 14 Q. I asked you about the 15 company-specific factors. 16 A. Okay. 17 Q. That's what I said. 18 A. Okay. And I'm turning to -- 19 Q. And I want to know what the 20 company-specific factors are that you looked to 21 in this study. 22 A. And page 9, Section B, is entitled 23 "Company-specific factors." 24 Q. Okay. Does it make reference to 25 any exhibit?

20 (Pages 74 to 77)

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 A. Let me look. Exhibit 7 and	2 company.
3 Exhibit 9 and Exhibit 8 are the exhibits that	3 I believe there's statistics in
4 are referenced in that section. But there's	4 the Hillion and Vermaelen paper that says if
5 also a lot of other information in the text	5 you issue more than one FPS on average, there's
6 that doesn't need an exhibit.	6 a very high likelihood that you're going into
7 Q. No, I understand that. But the	7 bankruptcy in the next -- in the next year.
8 "Company-specific factors," does it make	8 Q. Is that just --
9 reference to an exhibit in that section to	9 A. And that is -- all this chart says
10 support the statements about company-specific	10 is look at how many FPSs this company issued
11 factors?	11 since its IPO. And, in particular, getting
12 A. And I've just told you that	12 close to the issuance of the Series G in
13 there are three exhibits referenced in that	13 November 2000.
14 section.	14 This company was so risky it
15 Q. Okay. Let's take a look at seven.	15 couldn't get money from anywhere.
16 A. But I want to make sure that	16 Q. So, therefore, it justified
17 that's not the only information -- I want to	17 anything that Badian did to its stock. Is that
18 make sure you understand that that's not the	18 your conclusion?
19 only information we're relying on. We're	19 A. No, that's not my conclusion at
20 relying on the entire section in the report	20 all. My conclusion is this company was
21 which talks about a lot of other factors that	21 extremely risky and -- by indication of its
22 are not in exhibits.	22 numerous issues of FPS securities. And,
23 Q. All right. With that	23 therefore, any investor buying those securities
24 qualification, take a look at Exhibit No. 8.	24 had better have a good strategy to hedge
25 A. Yes.	25 against those risks. Otherwise, he's going to
Page 79	Page 81
1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 Q. These are specific events. Right?	2 lose his shorts.
3 A. Yes.	3 Q. Even if he violates a contract
4 Q. Did you do an event study on any	4 provision? Assuming --
5 of them?	5 A. I'm sorry, is there a question
6 A. No, I did not.	6 pending?
7 Q. In Pet Quarters, didn't you	7 Q. Assuming that there was a clear
8 criticize the plaintiff's expert report because	8 violation of the contract provision, is what
9 they pointed to company specific -- specific	9 you're saying is he better short the stock even
10 events and they failed to do event studies?	10 if he's contractually agreed, clearly and
11 A. You'd have to show me the specific	11 unequivocally, not to do so? Is that your
12 section of the Pet Quarters report to remind me	12 testimony?
13 of that.	13 MR. SOHN: Is that a question?
14 Q. I --	14 MR. GUIDO: That is a question.
15 A. The point of this chart is not to	15 A. Well, now we're talking about this
16 do an event study on what happened to the stock	16 specific case and --
17 price when a convertible issued. The point of	17 Q. I --
18 this chart is to show that Sedona was a serial	18 A. -- my -- and my understanding is
19 FPS issuer. This company couldn't raise money	19 that's not an allegation in the SEC --
20 anywhere except through future price	20 Q. I didn't ask you --
21 securities.	21 A. It's not an allegation in the SEC
22 That is a terrible indictment of	22 complaint.
23 the financial performance and the ability of	23 Q. I didn't ask you whether it was an
24 that company to raise money, and is an	24 allegation in the complaint and that that's a
25 indicator of the extreme riskiness of that	25 legal judgment --

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	A. Well --	2	you want me to address?
3	Q. -- and you said you were not	3	Q. I want you to answer, you know,
4	making legal judgments. Put the Complaint	4	whether or not it's a legitimate economic
5	aside. I'm asking you a question about a fact,	5	strategy as you've used the term. You've used
6	not about the Complaint.	6	the term.
7	A. And what is the question?	7	MR. SOHN: Objection.
8	Q. And the question is: Does the	8	Q. So please answer the question
9	condition of Sedona -- based on your statement	9	based on your use of the term.
10	about Chart 8 is an indictment of Sedona's	10	A. Factoring in now your -- your
11	performance, does that justify Badian violating	11	assertion that this is a clear violation of the
12	a clear-cut contractual provision? Assuming	12	contract --
13	it's clear-cut.	13	Q. A contract provision.
14	MR. SOHN: Mr. Guido, two things:	14	A. A contract provision?
15	One, I'm going to object to your question; two,	15	Q. That's correct.
16	your voice is going up a little bit.	16	A. Well, it may be.
17	MR. GUIDO: Well, I'm sorry, I'm	17	Q. It may be?
18	trying to help the court reporter. She	18	A. It may be a legitimate strategy.
19	complained about my soft voice. Okay?	19	Q. Okay. Under what circumstances is
20	MR. SOHN: We're going to work for	20	it a legitimate strategy to violate a clear
21	a middle ground.	21	contractual term?
22	A. And I have one clarification.	22	MR. SOHN: Objection. This is
23	It's not just Chart 8 that indicates the poor	23	like the tenth time that we've gone through
24	performance of Sedona. There's a lot of other	24	this.
25	charts in there.	25	A. Yeah, we weren't asked to address
	Page 83		Page 85
1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	Q. Okay.	2	that issue and I can't give you an answer to
3	A. But, in addition, we weren't asked	3	all the conditions that would be in place.
4	to address that issue. So I don't have an	4	That's not something that we were asked to
5	opinion on it.	5	address as it's clear in our -- in our report.
6	Q. Well, I mean, you -- you used --	6	Q. Is there anywhere in your report
7	you used the term when I just asked you. You	7	where you indicate that you're not taking into
8	used the term "legitimate strategy." I'm just	8	consideration the contract terms?
9	trying to find out what you're saying.	9	A. What is indicated in our report is
10	A. And my -- my answer is that a	10	the tasks we were asked to answer, the
11	legitimate strategy is an optimal strategy to	11	questions we were asked to answer.
12	hedge an FPS. And what we see Rhino doing is	12	MR. GUIDO: Okay. Why don't we
13	that optimal strategy.	13	take a break. We'll get to the questions.
14	Q. Even if it's a violation of a	14	THE VIDEOGRAPHER: This concludes
15	clear-cut contractual provision?	15	Tape Number 1 in the videotaped deposition of
16	A. My understanding is that's not an	16	Mr. Stephen Prowse. Going off the record at
17	issue in this case. And --	17	11:52 a.m.
18	Q. And --	18	(A recess is taken.)
19	A. -- we specifically weren't asked	19	THE VIDEOGRAPHER: This begins
20	to address it.	20	Tape Number 2 in the videotaped deposition of
21	Q. Okay. So now I'm asking you to	21	Mr. Stephen Prowse. Going back on the record
22	address it.	22	at 12:01 p.m.
23	A. And --	23	BY MR. GUIDO:
24	Q. You're the expert.	24	Q. Now, I think you testified before
25	A. And how do you want me -- what do	25	we went off the record that another one of the

22 (Pages 82 to 85)

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 factors that you considered in reaching your</p> <p>3 conclusion there was no more manipulation was</p> <p>4 that Sedona's performance over time explained</p> <p>5 by the market, the lack of the market, and the</p> <p>6 peers. Is that correct?</p> <p>7 A. Correct.</p> <p>8 Q. Okay. Did you do a statistical</p> <p>9 regression analysis against the new market</p> <p>10 indices?</p> <p>11 A. We did a regression analysis that</p> <p>12 included the NASDAQ as the -- one of the</p> <p>13 independent variables, correct.</p> <p>14 Q. Where -- where -- where in the</p> <p>15 exhibits can I find that?</p> <p>16 A. For example, Exhibit 13A.</p> <p>17 Q. Okay. And where is --</p> <p>18 A. Or 13B.</p> <p>19 Q. Pardon?</p> <p>20 A. Or 13B.</p> <p>21 Q. Or 13B or both?</p> <p>22 A. Or both.</p> <p>23 Q. Now, how can I tell looking at 13A</p> <p>24 whether there's a statistical significance of</p> <p>25 the relationship between Sedona stock and --</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 happened to the NASDAQ stock price, in terms of</p> <p>3 a return, and then correlating the two through</p> <p>4 regression.</p> <p>5 Q. Okay. And in the correlating and</p> <p>6 through regression, do you average out those</p> <p>7 price changes over that time period to come up</p> <p>8 with a figure to compare it?</p> <p>9 A. No.</p> <p>10 Q. You use every day?</p> <p>11 A. It's a day-to-day comparison,</p> <p>12 correct.</p> <p>13 Q. All right. Now -- and it shows</p> <p>14 that there is a statistically significant</p> <p>15 relationship between the NASDAQ return and the</p> <p>16 Sedona return in 13A?</p> <p>17 A. It shows the "P" values are less</p> <p>18 than .01.</p> <p>19 Q. Okay. Which is 99 percent</p> <p>20 significant?</p> <p>21 A. That's -- that's looking at each</p> <p>22 regression on a stand-alone basis. Correct.</p> <p>23 Q. I understand.</p> <p>24 Now, take a look at 13B. That's</p> <p>25 March 1, 2001 through May 31st, 2009. The</p>
Page 87	Page 89
<p>1 - STEPHEN D. PROWSE -</p> <p>2 stock price movement and NASDAQ's price</p> <p>3 movement?</p> <p>4 A. Well, if you were looking at these</p> <p>5 on a stand-alone basis, you'd look at the star</p> <p>6 indicators.</p> <p>7 Q. Okay. And that does -- under</p> <p>8 "NASDAQ return," does that double star denote a</p> <p>9 significance in the relationship between Sedona</p> <p>10 -- Sedona's stock price movement and NASDAQ</p> <p>11 price movement?</p> <p>12 A. Just looking at that one</p> <p>13 regression, the "P" value is greater than -- or</p> <p>14 less than .01.</p> <p>15 Q. Okay. So -- and -- so how -- I</p> <p>16 mean, how was that analysis done? What were</p> <p>17 the variables? Was it every day over this time</p> <p>18 period of June 26th 2000 to June 14th, 2002, or</p> <p>19 was it just the beginning and end time?</p> <p>20 A. No, it was daily data.</p> <p>21 Q. Daily data?</p> <p>22 A. So it was a regression analysis</p> <p>23 using however many trading days there are in</p> <p>24 that period, going from day to day, seeing what</p> <p>25 happened to Sedona's stock price, seeing what</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 NASDAQ return there doesn't have any asterisks.</p> <p>3 What does that signify?</p> <p>4 A. That signifies that the "P" value</p> <p>5 is greater than .05.</p> <p>6 Q. Okay. And does that indicate, in</p> <p>7 your opinion, that it lacks statistical</p> <p>8 significance?</p> <p>9 A. That's correct. It lacks</p> <p>10 statistical significance.</p> <p>11 Q. Now -- so that for the time period</p> <p>12 March 1 through May 31st, 2001, is it fair to</p> <p>13 conclude that you have not shown that Sedona's</p> <p>14 stock price was influenced by the NASDAQ</p> <p>15 return?</p> <p>16 A. You can't reject the hypothesis</p> <p>17 that the coefficient is zero.</p> <p>18 Q. Or that you can't reject the</p> <p>19 hypothesis that there's no relationship?</p> <p>20 A. You can't reject the hypothesis</p> <p>21 that there's no relationship.</p> <p>22 Q. Now, I'd like to also direct your</p> <p>23 attention to another exhibit which there was a</p> <p>24 -- that you chose to put in the exhibits and</p> <p>25 that is Exhibit 5A.</p>

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	I think you indicated that the --	2	A. Well, I don't have a color copy of
3	that the Sedona stock performance was an	3	the chart.
4	indictment of it and, therefore, it explained	4	MR. SOHN: [Handing document to
5	that any impact on its price was not due to	5	witness].
6	market manipulation.	6	A. Okay. So, Sedona is red. Well,
7	And I'd like to direct your	7	it's hard to tell what it did without drawing
8	attention --	8	lines on for the two dates you mentioned, which
9	A. No, I didn't say that.	9	were March 1st and March 31st?
10	Q. I'm sorry. Well, you did give a	10	Q. March 1st through May 31st.
11	quite lengthy response in which you did	11	A. March 1st through May 31st. Okay.
12	indicate that Sedona's stock -- stock price	12	March 1st through May 31st. It looks like it
13	performance and its characteristics was an	13	went up, but -- overall, on average, but just
14	indictment, didn't you, of something?	14	eyeballing it, it doesn't look like it doubled
15	MR. SOHN: Objection.	15	to me.
16	A. I said -- I said --	16	Q. Well, it did go from 20 to
17	Q. And what was that something?	17	somewhere short of 40, didn't it?
18	A. I said that its operating	18	A. At some point in time, but I'm not
19	performance as -- and then as reflected, I	19	sure where that is relative to May 31st.
20	believe, in its stock price volatility, its	20	Q. Well, let me ask you something.
21	stock price decline, and -- and the fact that	21	You used the time period of June 26, 2000
22	it relied almost solely on, or very largely on,	22	through June 14th, 2002, and you used March
23	FPS issues to raise money was indicative of it	23	1st, 2001 through May 31, 2001, but -- for most
24	being a very risky stock.	24	of your other charts. But for some reason when
25	Q. Okay. Now, take a look at Exhibit	25	you talk about stock price performance versus
	Page 91		Page 93
1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	5A. 5A, the Sedona price returns were in red.	2	peer group companies and NASDAQ, you don't do
3	And look at the time period from -- the chart	3	it for that time period, do you?
4	doesn't address the May 1 -- March 1 through	4	A. No, we don't.
5	May 31st, '01, but the chart seems to indicate	5	Q. Why not?
6	that the price of Sedona during that period of	6	A. I don't know. We talk -- I think
7	time increased from a factor of about whatever	7	we talk about it in the report. The report
8	this factor is on the left of 20 to somewhere	8	numbers are actually in the body of the report.
9	just short of 40.	9	Q. Where is that?
10	What do those numbers mean on the	10	A. But --
11	left of this chart?	11	Q. Where?
12	A. These are -- this is just an	12	A. Let me see.
13	index. So all the -- the three stock price	13	Q. Look at paragraph 37 in --
14	indices -- the three stock price measures we're	14	A. Paragraph 37.
15	using here are all normalized to be the same on	15	Q. But that talks absolute prices.
16	June 26, 2000.	16	It doesn't talk about corrected prices, like
17	Q. Okay.	17	you did for Exhibit 5A, does it?
18	A. And, so, basically you're	18	A. Well, I'm not sure what you mean
19	comparing how the NASDAQ, Sedona and the peer	19	by "corrected prices."
20	group stock price performed since 2006 -- since	20	Q. Well, you said that you
21	June 26, 2000, relative to each other.	21	normalized --
22	Q. Okay. Well, does it indicate that	22	A. Right, but that wouldn't change --
23	the stock price of Sedona between March 1, 2001	23	that wouldn't change anything.
24	and May 31st, 2001, appears to have almost	24	Q. Okay. Well, it says --
25	doubled in value?	25	A. That wouldn't change anything.

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1	<p style="text-align: center;">- STEPHEN D. PROWSE -</p> <p>2 Q. Where is the data that supports 3 paragraph 37?</p> <p>4 A. Well, the -- you have the data 5 that supports paragraph 37.</p> <p>6 Q. Where is that?</p> <p>7 A. It's in the work sheets that were 8 produced to you.</p> <p>9 Q. No, I mean in the report. In the 10 report.</p> <p>11 A. Well, we didn't -- we didn't 12 produce all of the data that support all the 13 numbers in here. Most of the data's in the 14 work sheets.</p> <p>15 Q. Really? Hmm. 16 Now, --</p> <p>17 A. In fact, this data shows that the 18 stock price declined over this period that you 19 were talking about.</p> <p>20 Q. Well, then why did you put 5A in? 21 What is the purpose of 5A, that shows an 22 increase in the normalized -- or the adjusted 23 back to 6/26/2000?</p> <p>24 A. I don't know. I'd have to look at 25 the data -- I'd have to look at the data behind</p>	<p style="text-align: center;">- STEPHEN D. PROWSE -</p> <p>1 A. Yes.</p> <p>2 Q. Okay. Is this the -- the document 3 that you relied upon to prepare Exhibit 13B in 4 your expert report?</p> <p>5 A. I don't know where this comes 6 from, 13 -- this exhibit.</p> <p>7 Q. Well, I'll represent to you it 8 comes from a file called BP-4 and it's Tab 9 13B.</p> <p>10 A. Okay.</p> <p>11 Q. In the documents that were 12 produced by your office to the SEC.</p> <p>13 A. Okay.</p> <p>14 Q. Okay? Now, is that the document 15 that you reviewed to prepare the 13B that is in 16 your report?</p> <p>17 A. No, I didn't review this document.</p> <p>18 Q. Okay. Now, did you -- you know, 19 when you did the report, okay, what did you 20 review?</p> <p>21 A. What I --</p> <p>22 Q. In terms of data.</p> <p>23 A. In terms of data?</p> <p>24 Q. Uh-huh.</p>
1	<p style="text-align: center;">- STEPHEN D. PROWSE -</p> <p>2 Exhibit 5A to understand what's going on, which 3 is in the work sheets.</p> <p>4 Q. Do you know?</p> <p>5 A. And, you know, I made a decision 6 not to -- not to include every single piece of 7 analysis we did as an exhibit to the report. 8 That would have been overkill. I would have 9 had --</p> <p>10 Q. Overkill or data mining?</p> <p>11 A. No, it would have been overkill.</p> <p>12 Q. Now, --</p> <p>13 A. We didn't do any data mining.</p> <p>14 MR. GUIDO: I'd like to have 15 marked as Exhibit No. 23 a rendition of Exhibit 16 13B.</p> <p>17 MR. SOHN: Did you say "a 18 rendition of"?</p> <p>19 MR. GUIDO: That's what I said, 20 which is extracted from BP-4.</p> <p>21 (Whereupon, exhibit is received 22 and marked BP-23 for identification.)</p> <p>23 BY MR. GUIDO:</p> <p>24 Q. Do you have Exhibit 23 in front of 25 you?</p>	<p style="text-align: center;">- STEPHEN D. PROWSE -</p> <p>1 A. I reviewed the exhibits as they 2 were in -- as they were reported.</p> <p>3 Q. Okay.</p> <p>4 A. And I re -- and I had discussions 5 with Erica Rose about the results of all the 6 statistical analyses that we did on the Sedona 7 matter.</p> <p>8 Q. Okay. And let's take the text of 9 the report.</p> <p>10 Who wrote the initial draft?</p> <p>11 A. I believe the initial draft was 12 written by Mr. Beloreshki. I'm not sure when. 13 Prior to me getting involved in the -- in the 14 engagement. But I took over the writing of the 15 draft because, in November of 2009, we didn't 16 have a whole lot of time to get the report out. 17 And, so, I had -- I had spare time and 18 Mr. Beloreshki didn't. So I took over, 19 basically, the editing of the draft and the 20 writing of the draft.</p> <p>21 Q. Well, take the second to the last 22 paragraph in the -- in the report.</p> <p>23 Did you edit that paragraph?</p> <p>24 A. I can't remember. I can't</p>

25 (Pages 94 to 97)

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 remember if I edited it or not.</p> <p>3 Q. Well, when you edited the draft,</p> <p>4 did you review your edits with anyone?</p> <p>5 A. Did I review my edits?</p> <p>6 Q. Uh-huh.</p> <p>7 A. Mr. Beloreshki would have seen,</p> <p>8 and probably Erica would have seen, the final</p> <p>9 version before it went out, yes.</p> <p>10 Q. Well, from the day you got this</p> <p>11 draft and you started the editing process, who</p> <p>12 did you deal with about the draft?</p> <p>13 A. I dealt with Mr. Beloreshki and</p> <p>14 Erica Rose.</p> <p>15 Q. Anyone else?</p> <p>16 A. Perhaps we may have had a staff</p> <p>17 person in Dallas working on this, as well,</p> <p>18 Mr. Blanton.</p> <p>19 Q. Have you had a conversation with</p> <p>20 anyone from DLA Piper?</p> <p>21 A. Yes, we had conversations with DLA</p> <p>22 Piper.</p> <p>23 Q. And how often did you have these</p> <p>24 conversations?</p> <p>25 A. Specific to the draft?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 this case.</p> <p>3 Do you recall that?</p> <p>4 A. Yes.</p> <p>5 Q. In fact, it was served on you at</p> <p>6 home, right, as I recall?</p> <p>7 A. Actually, it was not served on me.</p> <p>8 It was served on my wife.</p> <p>9 Q. On your wife?</p> <p>10 A. And my older daughter.</p> <p>11 Q. And your older daughter.</p> <p>12 A. Who were upset.</p> <p>13 Q. Yeah, I understand that. I heard</p> <p>14 that.</p> <p>15 And were you aware that the</p> <p>16 subpoena had been -- a processor had attempted</p> <p>17 to serve you at your office as part of that?</p> <p>18 A. I can't remember. I was traveling</p> <p>19 most of that week, so I wasn't in the office.</p> <p>20 Q. Did you -- did you give</p> <p>21 instructions to the people in the office not to</p> <p>22 accept subpoenas for you when you were not</p> <p>23 there?</p> <p>24 A. I didn't give any instructions.</p> <p>25 Q. Well, do you have standard</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Uh-huh.</p> <p>3 A. Probably not many. Maybe one at</p> <p>4 the end; maybe two at the end. I believe we</p> <p>5 probably had a WebEx set up.</p> <p>6 Q. What's a WebEx?</p> <p>7 A. Where they can look at the</p> <p>8 draft -- they go into our -- we send them a</p> <p>9 link to our server. They go in, they click on</p> <p>10 the link and go in and can look at the draft.</p> <p>11 Q. Does that include red lines?</p> <p>12 A. Can they see red lines?</p> <p>13 Q. Does your WebEx include red lines?</p> <p>14 When a draft appears on that WebEx, does it</p> <p>15 include red lines?</p> <p>16 A. I don't know. If there are red</p> <p>17 lines -- it shows that -- it shows literally</p> <p>18 the report. So if the report has red lines in</p> <p>19 it at that point, then it -- then it will show</p> <p>20 them.</p> <p>21 Q. But when you did your edits, did</p> <p>22 you do them as red lines?</p> <p>23 A. I can't remember whether I did</p> <p>24 them or not. Probably.</p> <p>25 Q. Well, you received a subpoena in</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 instructions?</p> <p>3 A. No.</p> <p>4 Q. Do you --</p> <p>5 A. I very rarely receive -- receive</p> <p>6 subpoenas.</p> <p>7 Q. Now, when you received the</p> <p>8 subpoena, did you attempt to determine what</p> <p>9 you had in your files in response to that</p> <p>10 subpoena?</p> <p>11 A. Yes. I spoke with in-house</p> <p>12 counsel, spoke with DLA Piper, spoke with</p> <p>13 Erica, and I believe I spoke with Tsvetan, as</p> <p>14 well, and we produced what documents we were</p> <p>15 asked to produce.</p> <p>16 Q. When did you produce those?</p> <p>17 A. Soon after receiving the subpoena.</p> <p>18 I can't remember the exact date.</p> <p>19 Q. Who did you produce them to?</p> <p>20 A. I think we put them on a disk and</p> <p>21 sent them to DLA Piper.</p> <p>22 Q. Did you have any role in putting</p> <p>23 any documents on a disk yesterday?</p> <p>24 A. I had a role in that I instructed</p> <p>25 Mr. -- a person in my staff to put some</p>

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1 - STEPHEN D. PROWSE - 2 documents on a disk and send it as a response 3 to a supplemental request, I guess, or 4 something for something that we hadn't produced 5 before that you wanted. So we put that 6 together and sent you a disk, which I 7 believe -- I'm not sure if you've gotten it 8 yet. That was happening either the day before 9 yesterday or yesterday.	1 - STEPHEN D. PROWSE - 2 just skipped over Exhibit 22. 3 MR. SOHN: I mean, 22 is 4 available. 5 THE REPORTER: Twenty-two -- 21 is 6 here. We premarked 21 and 22. All right? So 7 this is going to be another BP-22 then. 8 (Whereupon, exhibit is received and 9 marked BP-22 for identification.) 10 MR. SOHN: Thank you. 11 BY MR. GUIDO: 12 Q. Do you recognize Exhibit 22 as the 13 subpoena that was served upon you? 14 A. It looks like it. 15 Q. Okay. Now, it has a return date 16 of December 11th on it. 17 Do you see that? 18 A. Correct. 19 Q. Did you pull together the 20 documents before December 11th? 21 A. No, because -- I don't believe I 22 did. I think December -- I can't remember. I 23 think December 11th is -- it's either a Friday 24 or Saturday, I believe. And I think I received 25 the subpoena, or my wife and daughter received
1 - STEPHEN D. PROWSE - 2 ordered to produce the documents in the 3 subpoena? 4 MR. SOHN: Can we just be clear if 5 we're talking about the order, you know, the 6 evening order or the return date on the 7 subpoena? 8 MR. GUIDO: Yeah, I'm going to 9 give you that right now. Thank you, Mr. Sohn. 10 I'd like to have marked as an 11 exhibit, next number, the subpoena that was 12 serve on Mr. Prowse, or a copy of it. 13 I think we originally talked about 14 this as being Exhibit No. 23 when I talked to 15 the -- 16 MR. SOHN: You just marked 23, so 17 this should be 24. 18 MR. GUIDO: So it now has to be 19 24. 20 THE REPORTER: We premarked this 21 as Exhibit 23. 22 MR. SOHN: Why -- 23 THE REPORTER: I mean, I'm sorry, 24 we premarked this as Exhibit 22. So do you 25 want to rename it as Exhibit 22? Because we	1 - STEPHEN D. PROWSE - 2 the subpoena on Thursday night. And I was not 3 going to be in the office on Friday, so there 4 was no way I could get the documents together 5 in response to this subpoena. 6 So I immediately called my in-house 7 counsel, and they had, I believe, discussions 8 with DLA Piper. And I think at some point the 9 following week we produced the documents. 10 Q. Now, the -- you testified, with 11 regard to Exhibit 13B, the only rendition of 12 13B that you saw was the one that's in your 13 expert report, which is Deposition Exhibit 4. 14 MR. GUIDO: Mr. Sohn, can you give 15 the witness the copy of the expert report that 16 has the color highlighted? 17 MR. SOHN: Sure. 18 BY MR. GUIDO: 19 Q. Is Exhibit 13B from the 20 Deposition Exhibit No. 4 your Exhibit No. 24, 21 which was another rendition of Exhibit 13B? Is 22 that the document that you reviewed? 23 MR. SOHN: Mr. Guido, I think that 24 it's Exhibit 23, not Exhibit 24. 25 MR. GUIDO: Oh, excuse me.

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	MR. SOHN: Is that right?	2	done that?
3	MR. GUIDO: Yes.	3	MR. SOHN: Objection to form.
4	MR. SOHN: And I think you already	4	A. No.
5	asked the question, but...	5	Q. Did you discuss the regression
6	MR. GUIDO: Sorry.	6	results for Regression No. 5 with anyone before
7	BY MR. GUIDO:	7	you signed the expert report No. 4, which is
8	Q. Which one of these did you review	8	Exhibit No. 4?
9	when you signed the report?	9	A. Yes, I discussed all the
10	A. When I signed the report, I	10	regression results fairly early on in the
11	reviewed the one in the report.	11	analysis because this analysis is fairly easy
12	Q. Okay. And any time after you were	12	to run once you have the data up and running,
13	retained to participate in drafting the report,	13	which we did. So I discussed all of the
14	did you review Exhibit 23?	14	regression results with Erica Rose prior to
15	MR. SOHN: Objection. I think you	15	issuing the report.
16	already asked that question.	16	Q. The -- you discussed it with Erica
17	A. I can't -- no, not that I can	17	Rose?
18	remember.	18	A. Yes, who is a staff person working
19	MR. GUIDO: I'd like to have	19	with me on this engagement.
20	marked as exhibit next number, if somebody	20	Q. Okay. And what was your
21	would please tell me what the number is.	21	discussions with Erica Rose about Regression
22	THE REPORTER: Twenty-four.	22	Number 5?
23	MR. GUIDO: Twenty-four? Sorry.	23	A. Well, she told me, again, fairly
24	(Whereupon, exhibit is received	24	early on in the engagement, that of all the
25	and marked BP-24 for identification.)	25	regressions she ran, she got "P" values of
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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	BY MR. GUIDO:	2	greater than .05 for all of them except for
3	Q. Have you ever seen Exhibit 24	3	two, I believe, which I believe is Regression
4	before?	4	Number 5 and then one other.
5	A. I don't believe so, no.	5	Q. And that was Regression 4A, wasn't
6	Q. Do you know how Exhibit 23 --	6	it, initially?
7	Exhibits 23 and 24 came to be produced?	7	A. I don't know what it was
8	A. I'm sure they were in -- in the	8	originally. It's one -- it's the -- the other
9	work sheets that we produced to you.	9	one is the one that uses -- that doesn't use
10	Q. Did you know that Exhibit No. 23	10	the NASDAQ. It drops the NASDAQ out and uses
11	is the way the work sheet appeared in BP-4 when	11	net daily share transacted.
12	it was opened and examined?	12	Q. And that was the March 1st through
13	MR. SOHN: Objection to the form.	13	May 31st time period?
14	What is "it"?	14	A. Correct. So she told me that out
15	A. No.	15	of all the regressions she ran, she got a "P"
16	Q. Did you know that the Column T,	16	value greater than .05 on all of them except
17	the numbers in the Column T, were omitted from	17	for two.
18	the sheet as it appeared in the spreadsheet	18	And I made a mental note of that.
19	BP-04?	19	I thought, okay, I'm going to have to explain
20	A. No.	20	in the report why these two regre -- or drop a
21	MR. SOHN: Objection to form.	21	footnote and explain why these two regressions
22	Q. Okay. Did you know that anyone	22	don't change our opinion because of the correct
23	had applied the hidden function to that column?	23	adjustment you have to make when you're making
24	A. No, I do not.	24	multiple comparisons.
25	Q. So you don't know that anyone had	25	And I forgot to do that. I

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 forgot to drop the footnote in the final</p> <p>3 version of report to indicate that there were</p> <p>4 regressions run that had "P" values of greater</p> <p>5 than .05.</p> <p>6 And the final decision to make --</p> <p>7 which regressions to display was made towards</p> <p>8 the end of the engagement. And at that point I</p> <p>9 had forgotten what Regression Number 5 -- the</p> <p>10 results of Regression Number 5. And I</p> <p>11 mistakenly and, unfortunately, told Erica just</p> <p>12 report the first four, because I think they're</p> <p>13 a fair representation of what -- of the</p> <p>14 regressions we ran.</p> <p>15 And I forgot to draw -- I forgot</p> <p>16 to put a note in the report saying there were</p> <p>17 other regressions we ran. Two of them had "P"</p> <p>18 values greater than .05, but this doesn't</p> <p>19 change our opinion because of the adjustment</p> <p>20 you have to make.</p> <p>21 So Regression Number 5 not being</p> <p>22 included in the report was my fault, and I</p> <p>23 apologize for that.</p> <p>24 Q. All right. Take a look at --</p> <p>25 MR. GUIDO: Could you give the</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 included as exhibits, I had already determined</p> <p>3 I wasn't going -- I wasn't going to show as an</p> <p>4 exhibit every piece of analysis we'd already</p> <p>5 done.</p> <p>6 And, so, I decided -- I told Erica</p> <p>7 just report the first four, because I think</p> <p>8 that's a fair summary of what our regressions</p> <p>9 are. And I forgot to put a note in the -- into</p> <p>10 the report saying there were two other</p> <p>11 regressions of the 18 we ran that had "P"</p> <p>12 values of less than .05, but that that doesn't</p> <p>13 change our opinion.</p> <p>14 Q. Well, let me -- let me change the</p> <p>15 subject a little bit before I go any further</p> <p>16 with -- with this.</p> <p>17 And that is this BE/BF column --</p> <p>18 forget the report. BE/BF. It doesn't -- it</p> <p>19 doesn't describe that it's net daily trading</p> <p>20 absent NASDAQ.</p> <p>21 Why doesn't it have a description</p> <p>22 on those columns of what those calculations</p> <p>23 relate to?</p> <p>24 A. I don't know why.</p> <p>25 Q. Did you ever see it with the</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 witness the larger rendition of Exhibit No. 4</p> <p>3 to him?</p> <p>4 MR. SCHECHTMAN: Is that this?</p> <p>5 MR. SOHN: Yeah.</p> <p>6 MR. GUIDO: It's what is referred</p> <p>7 to as Tab 13B.</p> <p>8 BY MR. GUIDO:</p> <p>9 Q. I want you to take a look at the</p> <p>10 very last page of this.</p> <p>11 Are the columns BE and BF the</p> <p>12 regression that is net daily trades excluding</p> <p>13 NASDAQ?</p> <p>14 A. Are you asking me is that what the</p> <p>15 regression is?</p> <p>16 Q. Yes.</p> <p>17 A. I -- I believe it is.</p> <p>18 Q. Okay. So that's one of the others</p> <p>19 that you talked to Erica about excluding from</p> <p>20 the report?</p> <p>21 MR. SOHN: Objection to form.</p> <p>22 A. No, I didn't talk to her about</p> <p>23 excluding it from the report. If you remember,</p> <p>24 what I said was when the time came to formulate</p> <p>25 what exact statistical analysis would be</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 description?</p> <p>3 A. No, I never saw -- I never saw</p> <p>4 this data physically. I -- it was communicated</p> <p>5 to me verbally what the results were.</p> <p>6 Q. Because you never really looked at</p> <p>7 the data itself. You have only had people tell</p> <p>8 you verbally what the data showed. Isn't that</p> <p>9 correct?</p> <p>10 A. I've looked at the database that</p> <p>11 we're using and I've looked at some of the</p> <p>12 other results, but I didn't look at -- I</p> <p>13 didn't go into the database and look at the</p> <p>14 exact "P" values. They were communicated to me</p> <p>15 verbally.</p> <p>16 Q. So you -- you've never looked at</p> <p>17 the document that's been marked as Exhibit No.</p> <p>18 14?</p> <p>19 A. Oh, I have. I have since issuing</p> <p>20 the report, yes.</p> <p>21 Q. Since issuing. But prior to</p> <p>22 issuing your report, you didn't look at it, did</p> <p>23 you?</p> <p>24 A. I may have looked at the front</p> <p>25 part of the data which had the stock prices on</p>

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 them.	2 Q. Well, let me ask the question a
3 Q. Uh-huh.	3 different way.
4 A. But I don't remember going through	4 Do you think it's a significant
5 each regression and looking at each one.	5 omission from your report that you do not
6 Q. Now, in drafting the report -- let	6 address the other two regressions and explain
7 me see if I get this right -- you decided to	7 why you thought that they were not significant
8 exclude the regressions that showed a	8 for your conclusions?
9 significant correlation to the 95 percent	9 A. Yes, I do. It was a mistake and I
10 level?	10 should have noted it in the report that there
11 MR. SOHN: Objection to form.	11 was two regressions that we found that had "P"
12 A. I decided to include the first	12 values of less than .05.
13 four. And at the time I made that decision, I	13 Q. Now, I think you indicated that
14 had forgotten that there were two regressions	14 the last time that you read any literature on
15 that had a "P" value of greater than point --	15 micro kept (sic) structure was when you got
16 of than less than .05 on them.	16 your study for your -- what is it, the FCA?
17 Q. Now, let me ask you some	17 When you studied for your Ph.D.
18 questions.	18 A. That's actually not technically
19 Have you ever been involved in	19 correct, no.
20 accounting for a case measuring -- have you	20 Q. I'm sorry. I -- sometimes my
21 ever been involved in cases in which you've	21 memory fails me.
22 measured damages in a financial fraud or an	22 When did you -- when did you study
23 accounting fraud case?	23 microstructures?
24 A. Yes, I believe so.	24 A. I studied micro -- market
25 Q. And have you ever been involved in	25 microstructure as part of my Ph.D. training, as
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 one of those cases in which there was -- an	2 part of my CFA training. And in the time --
3 allegation of fraud involved the destruction of	3 and in those time -- so, in those time periods.
4 work papers?	4 Q. Now, in those time periods when
5 A. Maybe.	5 you studied it, did you study about the
6 Q. Maybe.	6 importance of how you structured the model to
7 So you're aware that accountants	7 reach conclusions based on regression
8 are required to retain their work papers even	8 analysis?
9 if they don't support their conclusions?	9 MR. SOHN: Objection to form.
10 A. I'm not -- I'm not aware of what	10 A. I can't recall specifics. But, in
11 the exact accounting requirements are. I'm not	11 general, structuring the model in any manner
12 an accountant.	12 is -- is important.
13 Q. Well, I mean, have you ever heard?	13 Q. And is it important that you have
14 I'm just asking if you ever heard.	14 a certain degree of expertise in that field for
15 A. I have a general understanding	15 which you were measuring the results in a
16 that accountants need to keep their work	16 regression analysis?
17 papers.	17 MR. SOHN: Objection to form.
18 Q. And do you have a general	18 A. Well, first of all, you have to
19 understanding that at one point in time there	19 have expertise in regression.
20 was a debate about whether or not they had to	20 Q. Okay.
21 keep their work papers that only supported	21 A. And, second of all, you have to
22 their conclusions as opposed to all of their	22 have expertise in general in the area, the
23 work papers that did not support their	23 general area that you're looking at, whether it
24 conclusions?	24 be financial economics, financial instruments,
25 A. I don't remember that.	25 financial markets.

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 Q. Well, is -- what is it about your	2 expert in statistics, is that person an expert
3 background that makes you think that you're	3 qualified to opine about whether the models
4 qualified to decide that two regressions that	4 that were used here were appropriate?
5 do not support your conclusions on their face	5 MR. SOHN: Objection to the extent
6 should be excluded from your report?	6 it calls for a legal conclusion.
7 MR. SOHN: Objection to the form.	7 A. Again, I'd have to know more about
8 A. Well, I've already testified that	8 your hypothetical. What I would say is if that
9 that was a mistake. And I would have -- and I	9 person has expertise in regression and
10 had forgotten that there were "P" values	10 statistical analysis, and also has demonstrated
11 associated with those two regressions that were	11 expertise in event studies and in understanding
12 less than .05.	12 how the stock price moves in response to
13 It doesn't -- my -- my	13 certain events, and has experience in analyzing
14 qualifications as being an expert in regression	14 financial markets, financial instruments,
15 or understanding what's significant and what's	15 applying statistical regression principals to
16 not are based on my training, my education, my	16 financial instruments and stock prices, I would
17 skills, my knowledge. I've been doing	17 say he's qualified.
18 regression analysis for 25 years. I've been	18 Q. Okay. What events in terms of
19 qualified as an expert to do regression	19 trading activity affects stock price moves in
20 analysis and to do event studies and to	20 your opinion?
21 understand the impact on stock prices of	21 MR. SOHN: Objection. Is this a
22 particular events.	22 general question?
23 So I think that's a short summary	23 MR. GUIDO: Yes. He just
24 of my qualifications to do a regression	24 testified what he thought was an important
25 analysis and understand the appropriate ways	25 characteristic.
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 to estimate stock price impact of certain	2 BY MR. GUIDO:
3 events.	3 Q. And I'm just asking what --
4 Q. Well, I just deposed a scientist	4 what -- you know, what factors in your view, in
5 who does regression analysis in determining the	5 terms of trading, affect stock price movements.
6 effect of the predictiveness of a protein	6 A. Well, I think you asked that
7 called P65 as a predictor of cancer. And he	7 question of me before. And I said there were a
8 knew a lot about statistics and he knew a lot	8 number of ways a trade as an event can affect a
9 about DNA analysis.	9 stock price. One is through information
10 Is he qualified to testify about	10 effects; two is through inventory effects on
11 whether or not these models are correct?	11 broker-dealer stocks. Those are at least two
12 MR. SOHN: Objection. I don't	12 channels through which a stock price -- a trade
13 know if that's -- if that's asking for a legal	13 can have impacts on a stock price. And I think
14 conclusion.	14 that's generally recognized.
15 BY MR. GUIDO:	15 Q. Well, in this case did you measure
16 Q. In your view.	16 inventory effect on stock prices?
17 A. I don't know enough -- I don't	17 A. No, we did not. We measured the
18 know enough about his background to make that	18 effect of the trade on the daily stock price
19 decision and.	19 change, which is a perfectly legitimate way to
20 Q. Just assume that that's all you	20 conduct an event study and measure the effect
21 know.	21 of a trade on -- or a number of trades on the
22 MR. SOHN: Objection.	22 stock price.
23 A. Then I can't -- then I'll -- then	23 Q. And you did six regressions, two
24 I'd say I don't know enough.	24 of which you discarded?
25 Q. Okay. If a person only was an	25 MR. SOHN: Objection.

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	A. We did 18 regressions, none of	2	hypothesis, which is that there is no impact.
3	which we discarded, all of which we included	3	Q. Okay. If the coefficient is
4	and considered.	4	significantly less than 75 percent, can the
5	Q. Let me -- let me shift a little	5	null hypothesis be rejected?
6	bit here and ask you another series of	6	A. That question makes no sense from
7	questions.	7	a statistical point of view.
8	When I deposed Mr. Beloreshki, I	8	Q. Can you say, based on these
9	found it a little confusing of what his answers	9	analyses, that the null hypothesis is true?
10	were. And I'm trying to get a better sense of	10	A. Statistics, any kind of
11	what a regression analysis means to you and to	11	statistics, cannot allow you to say the null is
12	him.	12	true. You cannot -- I'm sorry, let me back up.
13	And I guess my first question is:	13	You can either accept the null
14	What is the hypothesis that is being tested in	14	or -- you can either reject the null or fail to
15	these regressions?	15	reject the null hypothesis.
16	A. The hypothesis that is being	16	Q. Okay.
17	tested in this regression --	17	A. So if you reject the null -- if
18	Q. That are in your expert report.	18	you fail to reject the null hypothesis, that's
19	A. In these regressions, as well as	19	the best you can do.
20	the hypothesis that's being tested in the	20	Q. Okay.
21	parametric and the nonparametric statistics --	21	A. You can fail to reject the
22	Q. No, I'm asking you just about --	22	hypothesis that there's no impact of Rhino's
23	A. Well, they're the same. It's the	23	trading activity on the stock price. That's
24	same hypothesis.	24	the way I set up my tests. That's the way
25	Q. What's the same hypothesis?	25	Glosten and Jones set up their tests. That's
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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	A. It's the same hypothesis that	2	the way pretty much everybody in the academic
3	Professors Glosten and Jones used in their	3	literature who's ever done research sets up
4	analysis, which is the null hypothesis is that	4	their tests.
5	there's no impact.	5	MR. SOHN: Mr. Guido, I don't know
6	Q. So it's fair to say that the	6	if now is a good time, but we're --
7	hypothesis that's being tested is that there's	7	MR. GUIDO: What time do you have?
8	no relationship between Badian's activity and	8	MR. SCHECHTMAN: Ten to one.
9	the Sedona stock price?	9	MR. GUIDO: Ten to one? Okay.
10	A. The hypothesis that's being tested	10	We'll come back at 1:30?
11	is that there's no impact of the Rhino trades,	11	MR. SOHN: Okay. You didn't even
12	or whatever other measure of the trades is that	12	let me say what it's a good time for.
13	you want to use -- trading activity,	13	THE VIDEOGRAPHER: Going off the
14	transactions -- on the stock price. Exactly	14	record at 12:52 p.m.
15	the same as Professors Glosten and Jones' null	15	(A recess is taken.)
16	hypothesis, and exactly the same as the null	16	
17	hypothesis we used in our nonregression tests.	17	
18	Q. Now, is it fair to say that if the	18	
19	coefficient significant -- is significant at	19	
20	95 percent, the null hypothesis can be	20	
21	rejected?	21	
22	A. If the coefficient is significant	22	
23	at 95 percent, properly measured, with Alpha	23	
24	being the threshold "P" value properly	24	
25	measured, then you can reject the null	25	

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	A F T E R N O O N S E S S I O N	2	I -- have you been through the disk that -- the
3	THE VIDEOGRAPHER: Going back on	3	information you produced to DLA Piper after you
4	the record at 1:38 p.m.	4	received the subpoena?
5	BY MR. GUIDO:	5	A. I have not been through that disk.
6	Q. Mr. Prowse, in -- would you take a	6	Q. I have.
7	look at Exhibit No. 4 again, your report?	7	Is there anything in that that you
8	MR. GUIDO: Preferably if he	8	asked Erica to do that is not in that set of
9	could have the one that has the color, I	9	materials that you produced to the SEC?
10	would...	10	MR. SOHN: Objection.
11	BY MR. GUIDO:	11	A. Well, I haven't looked at the disk
12	Q. When you were retained to work on	12	you have, so I can't answer that a hundred
13	that report, did you direct anyone to engage in	13	percent. But all of the analyses,
14	any statistical or empirical studies?	14	statistical -- all of the analyses, as I
15	A. Yes, I think I testified earlier	15	understand it, were contained in a set of work
16	that I directed -- after discussions with	16	sheets that were produced.
17	Mr. Beloreshki, I directed Erica Rose to	17	Q. And they were prepared in 2003 and
18	perform statistical and econometric studies,	18	2004. Isn't that correct?
19	yes. Analysis.	19	A. I believe some of the old tabs
20	Q. Were they included in the text of	20	were done before I -- before we were retained
21	that report?	21	on this matter.
22	A. You had me on Exhibit 4. Now	22	Q. We --
23	you're talking about the text?	23	A. Before we --
24	Q. Just the whole text --	24	Q. Before we, FTI?
25	A. Oh, Deposition Exhibit 4?	25	A. Before we, FTI, were retained on
	Page 127		Page 129
1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	MR. SOHN: The deposition is	2	this matter when Mr. Beloreshki was at NERA.
3	Exhibit 4.	3	But regardless of what was done then, we redid
4	A. The deposition is Exhibit 4. I'm	4	or did anew all of the statistical analyses
5	sorry.	5	that we thought was required for this report.
6	So, sorry, could you repeat the	6	Q. Well, specifically what
7	question?	7	statistical analyses was done for the report,
8	Q. Well, when you were retained, and	8	Exhibit No. 4, after you were retained?
9	I think it was November 4th --	9	A. The statistical analyses breaks
10	A. Yes.	10	down into three groups: There is the
11	Q. -- did you direct anyone to	11	regression analysis, where we asked for 18
12	perform any statistical or economic studies at	12	regressions to be performed, nine in the
13	that point in time?	13	period -- the entire trading period for Rhino,
14	A. Yes.	14	and the same nine for a smaller period, March
15	Q. Who?	15	1st through May 31st, 2001.
16	A. Erica Rose.	16	Then we ad -- then we directed
17	Q. Okay. And what studies did you	17	tests to be run, nonparametric statistical
18	direct her to do?	18	tests and parametric statistical tests to be
19	A. I asked her to -- Tsvetan and I	19	run. Again, in those two periods; the longer
20	agreed on the statistical and regression	20	period that encompasses all of Rhino's trading
21	anal -- analyses and the various tests we	21	and the shorter period, March 1 through May 31,
22	wanted to run and the various nonstatistical	22	2001. And those tests were performed. And
23	analyses we wanted done. And we directed her	23	some, but not all, were actually reported in
24	to do all of that, and she did.	24	the report. But my understanding is all of
25	Q. Now, let me ask you a question:	25	the -- all of that analysis was produced.

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 Q. Well, I understand that. But take	2 A. Well, I'm not sure I understand
3 a look at Exhibit 14 again.	3 your question. I directed Erica Rose to do
4 Is there any regression in Exhibit	4 nine regressions in both periods. She reported
5 No. 14 that wasn't done prior to your retention	5 back to me the results of those nine
6 to sign on to Exhibit No. 4?	6 regressions.
7 A. Is there any regression that	7 Q. Okay. Now --
8 wasn't done --	8 A. In each period.
9 Q. -- prior to you being hired to	9 Q. Were any of those nine regressions
10 prepare the report, Exhibit No. 4.	10 different from the nine regressions you were
11 A. Well, I don't know exactly what	11 told had previously been performed?
12 was done prior to me being retained.	12 A. I wasn't told anything about what
13 Q. Okay. So, then, you don't know	13 was previously performed.
14 whether or not anything was done new after you	14 Q. I thought you told me that
15 were retained?	15 initially you were told nine regressions were
16 A. I know that everything was done	16 performed and you told them to go back and redo
17 new in the sense that the regressions were	17 them?
18 rerun. Even if they had been run -- even if --	18 A. No, I wasn't told -- no, I didn't
19 even if the same specification had been run on	19 say that. What I said was --
20 the same time period prior to our engagement,	20 Q. Well, the record will show what
21 prior to FTI's engagement, I know that that	21 you said.
22 regression was rerun after we were engaged.	22 A. -- that my understanding is that
23 Q. And --	23 some of the regressions that I asked to be run
24 A. So -- and the regressions and the	24 may have been run -- may have been run in a --
25 statistical analysis that were either done anew	25 prior to FTI being retained on this matter and
Page 131	Page 133
1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 or redone, I just described to you.	2 over a similar time period.
3 Q. Okay. Now, just take Exhibit 14.	3 Q. In Exhibit 14, okay, is there any
4 You said there's statistical regression	4 regression in here that you know had not been
5 analyses for March 1st through May 31. And	5 run prior to being retained?
6 there's a similar sheet for the longer time	6 A. I'm not sure. I don't believe,
7 period. Each of these regressions has certain	7 although I may be wrong, I don't believe that
8 variables included in it.	8 the period March 1 through May 31 was looked at
9 Did you participate in deciding	9 prior to FTI being retained. I may be wrong on
10 what the variables were to be included in each	10 that, but that's my belief.
11 of these regressions you had done?	11 Q. Okay. But that's a time issue.
12 A. I participated in deciding that we	12 Okay? I'm asking you about --
13 should run nine regressions and that -- and the	13 A. Right. A time period defines a
14 specification of those regressions.	14 regression.
15 Q. Okay. Let's take -- did	15 Q. Okay. Well, okay, fine. You
16 someone -- when you made that decision, did	16 didn't answer.
17 someone tell you that they had done nine	17 But putting the time period aside,
18 regressions and what the specifications were in	18 were any of the models for the regressions, can
19 those regressions?	19 you point to any of those that you directed be
20 A. Yes.	20 done after you became part of the team working
21 Q. Okay. And --	21 on the report that had not been done prior to
22 A. And what the results were.	22 the time you became a member of the team?
23 Q. Okay. And did you then tell them	23 A. My understanding is that the
24 to go back and redo those specific regressions?	24 models that Tsvetan -- that Mr. Beloreshki and
25 MR. SOHN: Objection to form.	25 I agreed were the appropriate models to be run

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1 - STEPHEN D. PROWSE - 2 were similar to the models that had been run 3 prior to FTI being retained. 4 Q. Do you know, can you tell us how 5 they differed in any way? 6 A. I can't -- I can't tell you that. 7 Q. Can you tell me that they did? Do 8 you think -- 9 A. I can't tell you that they did 10 differ. 11 Q. Now, the -- you indicated that you 12 also asked Erica to do economic analyses that 13 were different than the regression analyses 14 that are reflected in Exhibit No. 14. Is 15 that -- is that correct? 16 A. I believe what I said was -- I 17 asked for nonregression analysis to be done. 18 Q. Can you give us an example of what 19 you mean by a nonregression analysis by looking 20 at Exhibit No. 4? 21 A. For example, all of the analysis 22 in Section 3 of the report. 23 Q. That's paragraphs 34 through -- 24 A. Forty-eight. 25 Q. Through 50. Right?	1 - STEPHEN D. PROWSE - 2 understanding what market manipulation means. 3 Do you see the sentence, the last 4 sentence says, "In other words, the decline in 5 Sedona's stock price was consistent with 6 factors that were unrelated to the alleged 7 market manipulation by Rhino." 8 I used the term "Badian." We'll 9 use your term. 10 What do you mean by "the alleged 11 market manipulation"? What is the alleged 12 Market manipulation you're referring to 13 there? 14 A. I believe the alleged market 15 manipulation is referring to the allegations 16 that Rhino engaged in market manipulation to 17 move the stock price in certain directions. 18 Q. And what was the market 19 manipulation Rhino was alleged to have engaged 20 in based on your understanding of the 21 Complaint? 22 A. Well, their -- their Complaint's 23 not entirely clear as to the period that is 24 encompassed by the manipulation. There's a 25 variety of different periods that are talked
Page 135	Page 137
1 - STEPHEN D. PROWSE - 2 A. Oh, through -- through 50. 3 Correct. 4 Q. Okay. Now -- 5 A. And, in addition, there's other 6 nonregression analysis. 7 Q. Let's just stick with that. 8 A. Okay. 9 Q. There -- there are other 10 nonregression analysis they asked you to do. 11 But, first, is this analysis -- the analysis 12 that is reflected in 34 through 50. Okay? 13 Were any of those analyses, 14 analyses that had not been done prior to you 15 becoming a part of the team to prepare Exhibit 16 No. 4? 17 A. I don't know what had been done 18 prior and what hadn't. 19 Q. Okay. So you don't know whether 20 or not any of these were new? 21 A. I don't know whether any of these 22 were new in the sense that they had not been 23 done prior. 24 Q. Now, did you direct -- look at 25 paragraph 35. I'm back to my problem with	1 - STEPHEN D. PROWSE - 2 about. But I would say it goes from, maybe, 3 January '01 through April or May of '01. 4 Q. Okay. So that's one. Badian was 5 actually -- you use Rhino -- active during that 6 period of time. 7 And what activity do you 8 understand was manipulative during that time 9 period, or was alleged to have occurred in that 10 time period? 11 A. I think it's alleged that Badian 12 is alleged to have -- or that Rhino is alleged 13 to have traded in a manner to try to drive the 14 stock price down and to inject false 15 information into the market. I think that's 16 the allegations. 17 Q. Okay. Now, I read the Complaint. 18 I don't see where it says Rhino is the one who 19 pushed the price down. I see allegations that 20 Badian pushed the price down and Badian said 21 certain things at certain times. 22 Is the Complaint about Rhino or is 23 it about Badian? 24 A. I would have to look at the 25 Complaint to understand that. My understanding

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1 - STEPHEN D. PROWSE - 2 through counsel is that there's maybe a 3 complicated relationship with the various 4 trades and that we were just to assume that 5 Rhino -- we were just to use "Rhino." And I 6 think that's what we agreed upon in our initial 7 discussion.	1 - STEPHEN D. PROWSE - 2 A. I'd have to look at the Complaint 3 to be specific. 4 Q. You're not opining on Badian's 5 intent, are you? 6 A. No, I'm not -- I'm not opining on 7 Badian's intent. 8 Q. You're not opining anything on the 9 state of mind? 10 A. I'm not. 11 Q. I mean, so, when you use the term 12 "market manipulation," you're really talking 13 about affecting price movement. 14 Is that a fair characterization? 15 A. I think that would be a fair 16 characterization. 17 Q. Okay. 18 A. Affecting price movement. 19 Q. And, also, another use of the term 20 "market manipulation" is interjecting of false 21 information into the marketplace. 22 A. I think that's a -- I think that's 23 actually a legal requirement based on my lay 24 understanding of the law. 25 Q. Where'd you -- where'd you get
1 - STEPHEN D. PROWSE - 2 Q. Who asked you to use the term 3 "Rhino"? 4 A. Counsel. 5 Q. Which counsel? 6 A. I can't remember. Someone at DLA 7 Piper. 8 Q. Okay. Someone representing 9 Badian? 10 A. Someone representing Badian, 11 correct. 12 Q. Now, one of the allegations you 13 said is that Badian traded to push the price 14 down. Is that alleged in the Complaint? Is 15 that your understanding of the Complaint? 16 A. I would have to look at the 17 Complaint to be more specific, but I think one 18 of the allegations is that the trades were 19 alleged to have been -- were alleged to have 20 pushed the price down, yes. 21 Q. Okay. And it was alleged that 22 Badian intended to push the price down. 23 Is that your understanding? 24 A. I can't remember. 25 Q. Okay.	1 - STEPHEN D. PROWSE - 2 that understanding from of the law? From 3 Mr. Sohn? 4 A. No. 5 Q. From Ms. Schechtman? 6 A. No. Just general knowledge. 7 Q. Based on your reading ASTI, which 8 you asked Ms. Schechtman to send you? 9 A. Maybe reading ASTI, yeah. 10 Q. What about reading GFL? 11 A. I can't remember if I've read -- I 12 don't know what you refer to as GFL. 13 Q. Well, did you read Ms. Schechtman 14 and Mr. Beloreshki's piece before you prepared 15 your report? 16 A. Yes. 17 Q. Okay. Could you have gotten it 18 from that? 19 A. I don't know. I'd have to look. 20 Q. We'll take a look. 21 So, one of the questions in this 22 that you were addressing is whether or not 23 false information was reported to the market? 24 A. No, that's what -- you asked what 25 I thought was alleged in the Complaint, and I
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 think that is alleged in the Complaint.	2 Emerald account when you reviewed the trade
3 Q. So, when you say that there was no	3 data?
4 market manipulation, are you saying there was	4 A. Again, wash trades is a term that
5 no false information interjected into the	5 -- I think that's a legal or a tax term. I'm
6 marketplace here based on your analysis of the	6 not a tax expert. I'm not a legal expert. I
7 Sedona trades by Badian?	7 noticed some trades identified -- maybe alleged
8 A. I can't say that the -- the	8 as wash trades and maybe identified by Glosten
9 statistical analysis we do shows no support for	9 and Jones in their report as alleged trades.
10 that allegation.	10 So I'm aware of those -- I'm aware
11 Q. I see.	11 of those trades, if that's what you're asking.
12 Did you -- but I thought you said	12 Q. Well, what's your -- what's your
13 the statistical analysis just told you whether	13 understanding of the term "wash trade"?
14 the price moved or didn't move.	14 A. I have a very general, lay
15 A. That's correct. And if there's	15 understanding of a wash trade.
16 false information interjected into the market,	16 Q. Okay. And what is it?
17 you would expect the price to move.	17 A. A trade made by the same person, a
18 Q. Does the SEC have to show that the	18 buy and a sell, in order to reap some tax
19 price moves to bring a 10b case for injecting	19 advantage.
20 of false information into the market?	20 Q. So, in other words, it's a trade
21 MR. SOHN: Objection. This is a	21 by me in my account at what used to be Merrill
22 totally inappropriate question --	22 with me in my account at Schwab. Is that a
23 A. I don't know what -- I don't know	23 wash trade?
24 what the law is. I'm not a lawyer, so I can't	24 MR. SOHN: Objection.
25 speak to that.	25 Q. It's a hypothetical.
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 Q. Well, it sounded like that's what	2 A. Well, again, I'm not a tax expert
3 you were saying. I'm just asking you to	3 and I'm not a legal expert. So my
4 clarify.	4 understanding is either a trade made by -- a
5 A. No, what I'm saying is that the	5 sell followed by an immediate buy by me,
6 statistical analyses we do shows no support for	6 regardless of who the parties are, of the same
7 any -- any notion that Rhino's trades at any	7 stock in order to gain a tax -- tax advantage.
8 time influenced the price. One --	8 That's my -- that's my lay
9 Q. Did you look at --	9 understanding. I don't have a good legal
10 A. Can you let me finish, please?	10 understanding of what a wash trade is. I know
11 MR. SOHN: Mr. Guido, he is --	11 there are some alleged wash trades in the
12 Q. I'm sorry.	12 Complaint and I know what they are and I know
13 A. Can you let me finish?	13 they've been identified.
14 Q. I'm sorry.	14 Q. Didn't you claim to be an expert
15 A. I'm sorry, you'll have to -- could	15 at the outset of your testimony on financial
16 you read me back my answer?	16 markets?
17 (Whereupon, the record is read	17 A. Financial markets, financial
18 back.)	18 instruments, financial risks associated with
19 A. Influenced the price. And	19 financial instruments. The risks associated
20 presumably the only way false information --	20 with small firms raising finance. Yes, all
21 false information injected into the market can	21 that.
22 work is if it moves the price.	22 Q. What about an expert in trading
23 Q. Well, let me ask you something:	23 -- trading in financial instruments? Are
24 Did you -- did you see any wash trades between	24 you an expert in trading in financial
25 the Westminster Emerald account and the Refco	25 instruments?

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	A. I believe I have the expertise to	2	will -- it will account for the effect -- the
3	analyze the impact of trading, yes.	3	effect of both of them.
4	Q. Well --	4	Q. But it doesn't do a comparative
5	A. On the stock price.	5	analysis of the two?
6	Q. I mean, could one of the things	6	MR. SOHN: Objection to form.
7	that you might be curious about is whether or	7	A. It doesn't do a comparative
8	not trades are being reported between the same	8	analysis, no.
9	person?	9	Q. Thank you.
10	A. I know what those trades are --	10	Now, you -- you make some
11	MR. SOHN: Objection.	11	statements in here about you had Erica do some
12	A. -- and they were taken into	12	studies about non -- about market and industry
13	account in our analysis.	13	peer group factors. And one of the questions I
14	Q. They were?	14	think I asked you earlier is, had you done any
15	A. Yeah.	15	regression analyses on the relationship between
16	Q. Look at -- where do you see the	16	Sedona's stock price movement and the NASDAQ
17	Westminster to Refco trades taken into account	17	price movement? And you indicated you had and
18	in your expert report?	18	that for the longer period of time, it showed
19	A. We took account of all the trades	19	the statistical correlation, and for the
20	made by the accounts in this matter. And	20	shorter period of time it did not.
21	whether they were -- whether they were normal	21	Now, my question for you is, did
22	market trades, whether they were what you might	22	you do a similar analysis for the peer groups?
23	call wash trades. They're all in our data.	23	A. By "similar analysis" you mean
24	They're all in our data. So in our analyses	24	analysis -- a regression analysis involving the
25	they are taken into account.	25	peer groups?
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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	Q. Did you do a separate analysis of	2	Q. Uh-huh.
3	the wash trades to see what their impact was in	3	A. No, we did not.
4	the sells?	4	Q. Why not?
5	A. We didn't do a separate analysis,	5	A. I can't think of a particular
6	but we did an analysis with them in it.	6	reason why we didn't. I just can't think here,
7	Q. Did you do an analysis comparing	7	sitting here right now, what the reason was if
8	those transactions with other sets of	8	there was a reason.
9	transactions?	9	Q. Was the reason because the
10	MR. SOHN: Objection to the form.	10	capitalization was different in those
11	A. What are those transactions?	11	entities?
12	Q. In the -- take, for example, the	12	A. No.
13	wash trades between April 12th and April 19th,	13	MR. SOHN: Objection to form.
14	2001 between Westminster and Refco and	14	A. That wouldn't have been the
15	compare those to the transactions in October of	15	different -- that wouldn't have been the
16	2000.	16	reason. Capitalization of the NASDAQ is
17	MR. SOHN: Objection to the form.	17	different.
18	A. In the sense that they're all in	18	Q. Are there -- were there reasons
19	the database, yes, we did that.	19	because you couldn't develop a sufficient
20	Q. But --	20	database to do an analysis?
21	A. We took account of them.	21	A. I can't -- sitting here, I can't
22	Q. But the database doesn't compare	22	think of the reason why we didn't do that
23	the two, does it?	23	specific piece of analysis.
24	A. It includes them in the regression	24	Q. But you determined that it wasn't
25	analysis and in the statistical analysis, so it	25	going to be done?

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	A. For a reason I can't remember.	2	Q. Well, did you do an event study on
3	Q. But you did, for a reason, decide	3	the issuance of 10-Ks?
4	not to do it?	4	A. We did not do an event study on
5	MR. SOHN: Objection.	5	the issuance of 10-Ks. There wouldn't be a
6	A. For some reason.	6	reason to.
7	Q. Was it a good reason or a bad	7	Q. Did you do any event studies on
8	reason?	8	the company's issuance of equity securities?
9	MR. SOHN: Objection.	9	A. We did not do an event study on
10	A. Sitting here, I can't remember	10	the company's issuance of equity securities.
11	what the reason was.	11	Q. Did you do an event study on
12	Q. It was just a reason.	12	any -- any news releases from the company?
13	A. I can't remember what the reason	13	A. Actually, I want to qualify that
14	was.	14	last statement. To the extent that the equity
15	Q. But you did discuss it with	15	issuances were issuances of stock to Rhino, we
16	Ms. Beloreshki?	16	covered that in our database. So we looked at
17	A. Well, I can't remember -- I can't	17	that.
18	remember --	18	And, also, to the extent your
19	Q. Mr. Beloreshki, excuse me.	19	question covers issuance of stock due to
20	A. I can't remember discussing it	20	conversions, we looked at that, as well. So I
21	with Mr. Beloreshki. If I did remember	21	just want to qualify that last answer.
22	discussing it, I probably would have remembered	22	And then, with regards to question
23	more of the context around the discussion.	23	about news events, we did not do a study, an
24	Q. But you just didn't do it?	24	event study, regarding news events.
25	A. I just -- it's not here.	25	Q. I understand your answer, and I
	Page 151		Page 153
1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	Q. It's not here. Okay.	2	think I understood the reason for your answer
3	Now -- then you talk about the	3	to my question. But my question -- my
4	company-specific factors starting on page 9.	4	question, I think, hasn't been answered.
5	And I think I had asked you whether you did any	5	And my question is, did you do a
6	regression analysis to determine whether or not	6	specific event study on the issuance -- around
7	any of the events that you talked about had an	7	the issuance of securities by Sedona?
8	impact on the -- on the stock price. In the	8	MR. SOHN: Asked and answered.
9	event study, excuse me, that had an impact on	9	A. Yes, to the extent that -- to the
10	the price. And you indicated you had not done	10	extent that that covers Rhino's purchase of
11	that.	11	shares from Sedona and the conversions.
12	A. No, that's not correct. You were	12	Q. Well, is your answer yes, because
13	talking about Exhibit 8. And you had asked me,	13	you included it in the regression analyses that
14	Did you do an event study around the FPS	14	are in Exhibit No. 4?
15	issuance?	15	A. The regression analysis and the
16	Q. Okay.	16	nonregression analysis.
17	A. The serial FPS issuance that	17	Q. What's the --
18	Sedona went through throughout its life. And I	18	A. The statistical -- the parametric
19	said, no, we didn't do an event study there.	19	and nonparametric analysis, I believe. I
20	That wasn't the point of this chart.	20	believe that includes that, too. I'm not
21	Q. Okay.	21	sure.
22	A. We did do event studies, and	22	Q. Show me in Exhibit No. 4.
23	that's what the regression results are. They	23	A. Well, I believe that some of the
24	are event studies looking at the impact of	24	parametric tests we ran -- I would have to go
25	the -- of the Rhino trading.	25	back and check, but I believe some of the

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<p>1 - STEPHEN D. PROWSE - 2 parametric tests we ran cover conversions and 3 direct issuance of stock. I don't think any of 4 the ones reported in the -- in the exhibits to 5 Deposition Exhibit 4 do that, but I think some 6 of the other parametric or nonparametric tests 7 may do that.</p> <p>8 Q. But you can't point to anything in 9 this report, an event study on each of those 10 specific events?</p> <p>11 A. Well, this -- this wouldn't be an 12 event study. This would be a statistical 13 analysis of what happens to the stock price on 14 days when Rhino buys stock from Sedona. It 15 would be an analysis similar in concept to the 16 analyses in Exhibits 10 and 11, but it would 17 cover -- it would cover direct purchases or 18 conversions.</p> <p>19 So I'm not entirely sure, but I 20 think -- I think we may have done that in some 21 of the other non -- nonregression tests.</p> <p>22 Q. But it's not included in this 23 expert report, is it?</p> <p>24 A. There's not an exhibit that 25 reports the results of those non --</p>	<p>1 - STEPHEN D. PROWSE - 2 Q. And in Regression 3 in your 3 report, as I review the report, Regression 4 Number 3 talks about various files -- 5 A. Right. 6 Q. -- which were included in the 7 data, but there's no stand-alone regression 8 analysis for each of the stock issuances in an 9 event study to determine what that particular 10 event impact was on the price of Sedona stock, 11 was there? 12 A. There absolutely is, and that's 13 the coefficient under the Rhino principal in 14 Regression 3. That looks at the events of 15 Rhino buying principal. And that principal 16 includes two things: One, conversions; two, 17 direct purchases. 18 Q. What column is that? 19 A. Well, it depends how you count the 20 columns, but it's the column entitled "Rhino 21 principal" in quotation marks in Exhibit 13A 22 and 13B. 23 Q. I'm sorry, I'm asking you to look 24 at Exhibit 14. Tell me where. 25 A. Okay. So this may take a while.</p>
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<p>1 - STEPHEN D. PROWSE - 2 nonregression statistical tests. 3 Q. Oh, okay. 4 Do you know what the percentage of 5 significance was in those regression event 6 studies? 7 MR. SOHN: Objection to form. 8 A. Well, there's -- there's a 9 different "P" value for every regression, every 10 coefficient. So if you're asking me to recite 11 to you all the "P" values, I would have to go 12 and look at them to do that. So I'm not sure 13 what you're asking. 14 Q. Well, were there any "P" values 15 that were calculated for each of those events? 16 MR. SOHN: Objection to form. 17 A. Each of what events? 18 Q. The issuance of stock. 19 A. As a -- yes, there was, I believe. 20 Q. Is that in the documents that you 21 pulled together on that disk that you provided 22 to counsel after you received the subpoena in 23 this case? 24 A. No, it's in the results of 25 Regression 3 in the report.</p>	<p>1 - STEPHEN D. PROWSE - 2 Q. I'll make it easy for you. Look 3 at AQ. 4 A. AQ. Okay. So AQ looks to be 5 Regression 3. AQ. 6 Q. It's a subcategory of Regression 7 3, isn't it? 8 MR. SOHN: Objection to form. 9 Q. I think that's referred to as a 10 leading question, Mr. Prowse. 11 A. Sorry, I was trying to find the -- 12 find the right Regression 3 here. I'm trying 13 to match it up with -- oh, I'm probably looking 14 at the wrong exhibit here. 15 Q. You're look -- I mean, I've asked 16 you to look at Exhibit 14. 17 A. I am. I am. 18 Q. And I suggested you take a look at 19 Column AQ. 20 A. Yes, that's correct. That's 21 the -- that's the coefficient that is reported 22 in Exhibit 13B. 23 Q. Okay. 24 A. And that matches to Column AQ. 25 Q. Okay. Now, the principal in AQ,</p>

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1 - STEPHEN D. PROWSE - 2 okay, does that show that there's a 3 statistically significant correlation between 4 the issuance of stock and Sedona stock 5 prices? 6 A. It shows that there's not a 7 statistically significant relationship between 8 issuance of stock as I have defined it and 9 Sedona stock price. 10 Q. Okay. 11 MR. GUIDO: And why don't we take 12 a break. I think that the videographer needs 13 to change a tape. 14 THE VIDEOGRAPHER: This concludes 15 Tape Number 2 in the videotaped deposition of 16 Mr. Stephen Prowse. Going off the record at 17 2:16 p.m. 18 (A recess is taken.) 19 THE VIDEOGRAPHER: This begins 20 Tape Number 3 in the videotaped deposition of 21 Dr. Stephen Prowse. Going back on the record 22 at 2:24 p.m. 23 BY MR. GUIDO: 24 Q. The -- take a look at Exhibit No. 25 12, that Pet Quarters rebuttal report.	1 - STEPHEN D. PROWSE - 2 A. Correct. 3 Q. Okay. Would it be fair to 4 criticize your report for making allegations 5 about Sedona's stock price performance and its 6 financial condition and its issuance of 7 convertible debentures and the performance of 8 its peers in NASDAQ without doing a regression 9 analysis? 10 MR. SOHN: Objection; compound. 11 A. No, it wouldn't. 12 Q. Why not? 13 A. Well, in part because we do do a 14 regression analysis that takes into account 15 some of the variables you mentioned: NASDAQ, 16 issuance of stock and, the most important 17 variable, trades or transactions by Rhino. 18 The discussion that we have in 19 Section 3 of our report regarding other factors 20 that influenced Sedona's stock is meant to be 21 illustrative as opposed to, you know, 22 quantitative. 23 Q. Oh, okay. So you didn't attempt 24 to quantify, and you don't believe you had a 25 responsibility to do that, even though you said
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1 - STEPHEN D. PROWSE - 2 The -- do you recall preparing the 3 rebuttal report in Pet Quarters? 4 A. Yes. 5 Q. And do you recall that one of your 6 criticisms of the -- I -- you referred to it as 7 the Shapiro/Pham report, is that they had 8 failed to do regression analyses to support 9 their claims that certain events had an impact 10 on the market, or the price of Pet Quarters' 11 stock. 12 Do you recall that? 13 A. If you can direct me to where in 14 my report I say that, it would be helpful. 15 Q. Well take -- it's very easy. Take 16 a look at paragraph 7 of your report. 17 A. Yes. 18 Q. You see where you point out that 19 there's a need to do an event study if you 20 argue that any particular event had an impact 21 on -- on stock price? 22 A. Yes, I see that. 23 Q. And you criticize them for 24 Shapiro -- the Shapiro/Pham report for not 25 doing so?	1 - STEPHEN D. PROWSE - 2 that Shapiro Pham had a responsibility to do 3 that? 4 MR. SOHN: Objection. 5 A. Well, Shapiro/Pham -- I can't 6 remember exactly what Shapiro/Pham were doing, 7 but they didn't -- I think they were alleging 8 to estimate the response of a stock price to a 9 particular announcement. 10 Q. Well -- 11 A. We are -- I'm not finished. 12 Q. Excuse me. 13 A. We are in the context of doing an 14 event study. We do an event study with regards 15 to Rhino's trades in the context of pointing 16 out reasons why Sedona's stock price can be 17 expected to be, A, highly volatile, and, B, to 18 fall. 19 We are -- we are performing sort of 20 illustrative examples of the types of things 21 that would cause the stock price to be volatile 22 and to -- and to fall. 23 Q. You used illustrative examples 24 without doing a regression analysis of those 25 illustrative examples. And --

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 A. We did -- we did do a regression	2 Q. Yeah.
3 analysis of some of the variables you	3 A. I can't remember.
4 mentioned.	4 Q. You don't remember?
5 Q. In NASDAQ?	5 A. I'd have to review this report in
6 A. And issuance of stock.	6 detail and review the data. So, just reading
7 Q. And you found that there was no	7 this, I can't tell. But I do believe we're
8 statistically significant relationship between	8 looking at trades between accounts and we are
9 those two, between --	9 criticizing their analysis.
10 A. Between Rhino -- between issuance	10 Q. Okay. Well, I mean, paragraph 48
11 of stock to Rhino and stock price.	11 says that you're addressing the question of
12 Q. Now, the -- the other thing I	12 transactions between the respondents' own
13 found of interest in your rebuttal report was	13 accounts?
14 your critique of the Shapiro/Pham report's	14 A. Yes.
15 reliance on the certain kinds of trades. And	15 Q. And wasn't that a part of the
16 if you look at paragraph 48, I think is where	16 trading with itself?
17 you address that.	17 MR. SOHN: Objection to form.
18 I think that in this section	18 A. I'm not sure I necessarily agree
19 you're addressing the question of what are	19 with it. I used the language that I've used
20 known as wash trades; and that is trades	20 here. What's -- --
21 between accounts in which the same person is	21 Q. What's -- what's a respondent?
22 the beneficiary of it.	22 A. The respondent in this matter is
23 Is that a fair characterization of	23 the defendants.
24 what you're addressing in these paragraphs 48	24 Q. Okay. And the paragraph is
25 through 52?	25 addressing those defendants trading with
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 MR. SOHN: Objection to form.	2 themselves in two different accounts?
3 A. Forty-eight through 53? Did you	3 A. Transactions between defendants'
4 say 48 through 53?	4 own accounts. Correct.
5 Q. Well, okay, 53. I mean, I think	5 Q. Okay. And that you conclude that
6 it stopped -- for our purposes it stops at	6 the Shapiro/Pham report improperly concluded
7 paragraph 52. I think 53 addresses a different	7 that those transactions interjected false
8 issue.	8 information into the market that resulted in a
9 A. Well, I don't see the term "wash	9 price decline.
10 trades" anywhere in this section, so I'm not	10 Isn't that what you concluded?
11 sure what you mean by that.	11 A. We criticized their analysis.
12 Q. Well, it talks about trading	12 Q. Okay. And what was the critique
13 between matched buyers. Right?	13 of their analysis that you made?
14 A. It talks about respondents' trades	14 A. Well, it's detailed in paragraphs
15 between accounts.	15 50 through 52 or maybe 53.
16 Q. Okay. And are those between --	16 Q. Okay. Well, was one of your
17 were the facts in those cases the accounts were	17 criticisms that the transactions were
18 owned by the same party?	18 transactions that were executed at or near the
19 A. I -- I can't recall. It's been a	19 ask price as opposed to the bid price? And,
20 long time since I reviewed this report.	20 so, therefore the information interjected in
21 Q. Weren't those transactions between	21 the market tended to be positive for the price
22 Westminster and Refco Emerald accounts?	22 of Pet Quarters' stock?
23 MR. SOHN: Objection to form.	23 MR. SOHN: Objection to the form.
24 A. Are you talking about the Pet	24 A. I think we say the only way that
25 Quarters report?	25 they, the trades, might inject negative

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 information into the market would be if they	2 that if there was an intent by respondents in
3 were executed at prices below the bid at the	3 this matter, the Pet Quarters matter, to inject
4 time of the trade.	4 false information into the market, the
5 Q. Okay. Take a look at --	5 Shapiro/Pham report fails to offer an
6 A. So if their --	6 explanation for why all inter-account --
7 Q. Take a look at the very last page	7 inter-account transactions were not in the form
8 of Exhibit No. 12.	8 of sales.
9 A. Is that Exhibit 2?	9 If that was the intent, to inject
10 Q. Yes. What is Exhibit 2?	10 false information into the market, then why
11 A. Exhibit 2 is an exhibit which	11 aren't they all in the form of sales as opposed
12 shows some analysis regarding paragraph 52.	12 to nonmarket transfers?
13 Q. Okay. And are these intra-day	13 Q. So, I think what -- I'm a little
14 transactions?	14 puzzled by what you just said and let me -- let
15 A. Intra-day transactions?	15 me ask you a few questions.
16 Q. Yeah. I mean, is this evaluating	16 Now, what you're saying is, is
17 intra-day data?	17 that there couldn't have been false information
18 A. This is evaluating trades.	18 interjected into the market by nonmarket
19 Q. In relationship to what?	19 transfers?
20 A. To a bid-ask spread.	20 A. What I'm saying is if there was an
21 Q. The bid-ask spread when during the	21 intent to inject false information into the
22 day?	22 market, there's a failure to explain why all
23 A. I believe at the same time the	23 the accounts were not in the form of sales.
24 trade was made. I would have to --	24 Because that would seem to be the easiest way
25 Q. So this was --	25 to transmit information.
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 A. I would have to confirm that.	2 Q. Into the market.
3 Q. Okay. But it's your understanding	3 A. Into the market.
4 that that's what this does?	4 Q. Okay. And that would be important
5 A. That's my belief.	5 to know how the nonmarket trans -- transfers
6 Q. So is this an analysis of	6 interjected false information into the market?
7 intra-day trading?	7 A. It would be important to know if
8 A. This is an analysis of trades made	8 the market -- if the market transactions had an
9 with the -- with the bid-ask spread.	9 effect on the stock price.
10 Q. Okay. At -- at or near the time	10 Q. And it would be important to
11 of the bid-ask spread?	11 factor out the nonmarket transactions to
12 A. At or --	12 determine whether or not the market
13 MR. SOHN: Objection to the form.	13 transactions did have an impact?
14 A. At or near the time of trade.	14 A. That would be one way to do it.
15 Q. Now, paragraph 53 seems to be	15 And that's the way we do it, in fact, in our
16 talking about the Shapiro/Pham report's failure	16 analysis in the Sedona matter.
17 to exclude nonmarket transfers from its	17 Q. Well, which regressions that you
18 analysis. Is that a fair --	18 did that are included in your report exclude
19 A. No, it's not fair.	19 nonmarket transactions?
20 Q. -- inference to be drawn from that	20 A. So, I'm going to need to get my
21 paragraph?	21 report.
22 A. No.	22 MR. SOHN: Here.
23 Q. So, why was it important to say	23 A. So, if you turn to Exhibit 13 --
24 that there were three nonmarket transfers?	24 and you asked specifically about regressions
25 A. I think the intent here was to say	25 that excluded nonmarket transactions.

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1 - STEPHEN D. PROWSE - 2 Correct? 3 Q. That's correct. That's correct. 4 A. Okay. So that would be Regression 5 1, Regression 2, Regression 3 and Regression 4. 6 They all either exclude them or separate them 7 out. 8 Q. No, but the regression -- take a 9 look at -- take a look at Exhibit No. 14, which 10 is the backup for this, and tell me which one 11 of those columns of the regressions exclude 12 nonmarket transactions. 13 A. Well, we discussed this at length 14 in the morning. And I'm not sure what you mean 15 by "columns," but -- 16 Q. Well, I mean at the top it has the 17 letters at the top. That's what I mean by 18 columns. 19 Which one of your regressions 20 exclude nonmarket transactions? 21 A. Well, the regressions in this 22 Exhibit 14 that match up with Regression 1, 23 Regression 2, Regression 3 and Regression 4 in 24 Exhibit 13A or Exhibit 13B are the ones which 25 either exclude nonmarket transactions or	1 - STEPHEN D. PROWSE - 2 at spreadsheet 4. 3 MR. SOHN: I'm sorry, what are we 4 looking at? 5 MR. GUIDO: Exhibit No. 14. 6 Excuse me. 7 BY MR. GUIDO: 8 Q. And look at the Columns AS through 9 AW, just to clarify the record. 10 A. Okay. 11 Q. They're dealing with Regression 4 12 and an alternative to Regression 4, or 4A. 13 Do you see that? 14 A. Yes. 15 Q. Okay. Regression No. 4, which the 16 results are in Column A -- Column AT, are the 17 "Net daily shares transactions as percentage of 18 volume." And then AW says "Net trading as a 19 percentage of volume." 20 A. Right. 21 Q. In 4A. 22 So is it Column AW that's being 23 reported on the spreadsheet? 24 A. Yes. 25 Q. Okay.
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1 - STEPHEN D. PROWSE - 2 separate them out separately from market 3 transactions. 4 Q. Okay. Which ones exclude? Forget 5 the separate out. 6 A. The ones that exclude nonmarket 7 transactions are Regressions 1, 2 and 4. 8 Q. Look at Exhibit No. 15. 9 MR. SOHN: Fifteen? 10 MR. GUIDO: Fifteen. Deposition 11 Exhibit No. 15. 12 Q. And also look at Deposition 13 Exhibit Number -- 14 MR. GUIDO: Can I get back the two 15 most recent exhibits? 16 MR. SOHN: Twenty-four and -- 17 MR. GUIDO: Those. 18 MR. SOHN: Here are the most 19 recent ones. 20 BY MR. GUIDO: 21 Q. So it's one, two and four that 22 exclude the impact of nonmarket transactions? 23 A. They exclude nonmarket 24 transactions. 25 Q. Okay. The reason -- take a look	1 - STEPHEN D. PROWSE - 2 A. It's being reported in Exhibit 3 13B. 4 Q. Okay. Thank you. 5 Now, so, the Regression 1, 6 Regression 2 and Regression 4 do not include in 7 any way nonmarket transactions? 8 A. Yes, that's my understanding. 9 Q. All right. So we've got three 10 regressions. And let's take Regression 1. It 11 says "Any transaction flag." Okay? Do you see 12 that in Column AD, or on Exhibit 13B of your 13 expert report, it's the third column. It's 14 called "Any Rhino Trading." 15 A. Okay. So I'm looking at Column 16 AD? 17 Q. AD? 18 A. Yeah. 19 Q. In Exhibit 14. 20 A. Yeah. 21 Q. It says "Any Transaction Flag." 22 And that conforms with "Any Rhino Trading" 23 column on Exhibit 13B. Right? 24 A. No, it doesn't. 25 Q. It does not.

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 A. No.	2 on which there was a buy and a sell.
3 Q. Okay. What information in Exhibit	3 Q. Right.
4 14 -- what column corresponds to "Any Rhino	4 A. So it's appropriate to capture
5 Trading"?	5 that in both dummies, the buy dummy and the
6 A. The column in Exhibit 14 that	6 sell dummy.
7 corresponds to Regression 1 reported in Exhibit	7 Q. Okay. And -- and -- and how do
8 13B is Column AF and AG.	8 you use buy dummies as opposed to how do you
9 Q. AF and AG?	9 use sell dummies in your regression?
10 A. Yes.	10 A. Well, I use them the same. I
11 Q. Okay. All right. So it's a buy	11 mean, there's a buy dummy -- there's a buy
12 or sell flag?	12 dummy variable and there's a sell dummy
13 A. Yes.	13 variable. They are treated identically.
14 Q. Okay. And that is AF and AG.	14 Identically. They're independent variables in
15 Now, with regard to Regression	15 the regression.
16 Number 2, how does that differ from any Rhino	16 They're just -- they just have
17 trading?	17 different values on different days except
18 A. It separates -- separates out the	18 when -- except on days when Rhino doesn't do
19 effect of Rhino buys from Rhino sells and lets	19 anything, in which case they're both zeroes.
20 them have inde -- independent effects on the	20 And on days when Rhino sells and buys on the
21 price of Sedona to investigate whether	21 same day, in which case they're both one. But
22 specifically Rhino purchases as opposed to	22 that's --
23 Rhino sells, or vice versa, have any impact on	23 Q. Well --
24 the price.	24 A. That's no big deal.
25 Q. So, in other words, you do two	25 Q. -- in this regression are you
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 separate regressions and then you combine them?	2 comparing buy days against sell days?
3 Is that --	3 A. Where -- in this regression, which
4 A. No.	4 is Regression 2, we are looking -- Regression 2
5 Q. No? How do you do that	5 in Exhibit 13B. We are looking at whether
6 mathematically?	6 there is an indi -- an effect specific to Rhino
7 A. You just have a dummy variable	7 buys on Sedona stock price, and simultaneously
8 that is zero when Rhino does anything but buy,	8 we are looking at whether there is an effect
9 and a one when Rhino buys. That's a dummy or a	9 specific to Rhino sells on Sedona stock price.
10 buy flag.	10 Q. So this is not comparing the
11 Q. Okay.	11 results on days where there's a sell flag with
12 A. Then you have a dummy that is zero	12 the days where there are buy flags? This
13 for any other -- any time other than -- any day	13 Regression Number 2.
14 other than when Rhino sells, and one if Rhino	14 A. I don't know what you mean by
15 sells. And you just stick them in the same	15 that. You can -- you could compare the
16 regression.	16 coefficients of the Rhino buy dummy with the
17 Q. Well, take a look at line 645,	17 Rhino sell dummy if you wanted to, if that's
18 6/20/2000, and run it over to AJ and AK, where	18 what you mean.
19 it has these "dummies." And there are two	19 Q. Can I use any of these numbers
20 ones.	20 that you've -- that you've come up with under
21 A. Correct.	21 AJ and AK to figure out what that relationship
22 Q. How do you distinguish between the	22 would be?
23 two ones and those that have just a one in one	23 MR. SOHN: Objection to the form.
24 of the columns?	24 A. Relationship between what?
25 A. Well, that was a day, obviously,	25 Q. Between comparing sell days and

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2 buy days.	2 trades.
3 A. Well, you can either do that by	3 Q. Well, suppose that on one of those
4 looking at Column AJ or AK, or you can do that	4 days where you put a one is that Badian's
5 by looking at the two columns in Exhibit 13B	5 activity pushes the Sedona -- or as a result --
6 underneath Rhino purchases and Rhino sales.	6 or occurs at the time. Excuse me. The
7 One will be .01 point estimate of	7 causation, rather.
8 the coefficient, and one will be a negative .04	8 Suppose that on a day Badian's
9 point coefficient grounded. It's actually	9 activity -- Badian trades, and the price goes
10 .036, but -- negative .036.	10 down 5 percent and he had -- his activity
11 Q. Okay. So taking these days, okay,	11 involved the selling of five thousand shares.
12 what you're doing is that you're designating a	12 And on another day you have a one, and that he
13 day as a day when Badian was trading as opposed	13 trades/sells five hundred shares and the price
14 to days he was not?	14 goes down 1 percent.
15 A. That is what regression -- that is	15 Does this regression formula take
16 not what Regression 2 does. That's --	16 into consideration the impact of the size of
17 Regression 1 looks at the difference between	17 his sales?
18 when Rhino was trading and when Rhino was not	18 MR. SOHN: Objection to the form.
19 trading.	19 A. The regression does not take into
20 Q. Okay.	20 account the impact of the size of the trade.
21 A. Regression 2 looks at the	21 It takes into account whether there was a trade
22 difference between Rhino when -- between --	22 or not.
23 looks at the effect of when Rhino was selling	23 Q. When you -- are you aware that the
24 and then, separately, the effect of when Rhino	24 literature that addresses the question of the
25 was buying.	25 impact of trading on market price indicates
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 Q. Okay. Let's go back to -- let's	2 that the quantity, the size, of the sell or buy
3 focus on Regression 1 now.	3 activity should be included in the measurement
4 I gather the variable any day of	4 to determine a significant relationship between
5 trading indicates by a one the days that Rhino	5 price and trading?
6 or Badian traded Sedona stock. Is that	6 MR. SOHN: Objection to the form.
7 correct?	7 A. I'm generally aware that there are
8 A. The days when Rhino had a -- had a	8 some results that suggest that's a measure of
9 trade, right.	9 trading that could be used to measure the
10 Q. Okay.	10 impact of a trade, the size of it, or the size
11 A. Whether it was a buy or whether it	11 of it relative to volume. But I'm also aware
12 was a sell.	12 of numerous results that look at just whether
13 Q. Okay. And do the results indicate	13 there was a trade or not.
14 the coefficient that measures the difference in	14 Q. Well, I'm asking -- I mean, I'm
15 the average daily Sedona returns on the days	15 not asking you about results. I'm asking you
16 that Rhino traded compared to days that Rhino	16 about literature.
17 did not trade?	17 A. And I'm telling you about the
18 A. Could you repeat that question or	18 results that I see in the literature.
19 read it back?	19 Q. Okay.
20 MR. GUIDO: Would you read that	20 A. That there are results that stem
21 back, please?	21 from measuring the size of the trade or the
22 (Whereupon, the record is read	22 size of the trade relative to volume versus
23 back.)	23 there are other results that look at just
24 A. The coefficient measures the	24 whether someone is trading or whether there is
25 effect on Sedona's stock returns when Rhino	25 a trade.

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 Q. Well, let me ask you this	2 Q. And that sells at the bids have a
3 question. I've been going through this	3 tendency to push the price down?
4 material and going through the literature and	4 A. Again, I don't think I've
5 this term "power" comes up.	5 testified to that yet, but it's possible.
6 Can you tell me what the term	6 Q. Okay. And that this doesn't --
7 "power" of a regression method is?	7 this analysis in Regression Number 1 doesn't
8 A. Generally, the power of a	8 take into consideration either of those facts,
9 regression is the ability to detect a	9 does it?
10 relationship.	10 MR. SOHN: Objection to form.
11 Q. Okay. So that -- and do	11 A. It takes into account whether
12 different analyses or methods have different	12 Rhino's buying and -- and/or selling.
13 powers?	13 Q. It doesn't take into account, one,
14 A. They may.	14 the size of the transactions. Correct?
15 Q. Okay. And didn't the literature	15 A. Correct.
16 that you reviewed indicate that a regression	16 Q. And it doesn't take into
17 that includes the size of the transactions is	17 consideration whether or not the buys or sells
18 of greater power than one that does not?	18 were bids or asks, does it?
19 A. I'm not aware of that.	19 A. That's correct. It just looks at
20 Q. You're not aware of any literature	20 the overall effect.
21 that says that?	21 Q. Okay. Now, let's go to Regression
22 A. I'm not aware of that.	22 Number 2. I'm sorry to keep coming back to it,
23 Q. Okay. Now, the other is, is that	23 but I am very puzzled by -- by how you've
24 on -- when you have the variable "any Rhino	24 described the regression and how it's modeled.
25 trading," that doesn't distinguish between	25 Does this regression take into
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 whether or not Rhino bought or Rhino sold, does	2 consideration the size of the buys or sells in
3 it?	3 determining the effect of a share price?
4 A. No, it just looks at whether there	4 MR. SOHN: Objection to form.
5 -- there's an impact from Rhino being in the	5 A. No, it doesn't. It just takes
6 market.	6 into account whether there was a sell or
7 Q. So Rhino's in the market. It	7 whether there was a buy.
8 could go up or it could go down?	8 Q. Now, Regression Number 3, it has
9 A. Rhino's in the market. Is there	9 these additional variables: The transfers and
10 an impact from Rhino being in the market on the	10 the principals, for example.
11 stock price?	11 And is there any evidence in the
12 Q. Okay. And it doesn't measure	12 record of this case or in anything that's been
13 whether its activities are buy or sell. It's	13 provided to you that indicates either of those
14 just in the market?	14 events was information that was publicly
15 A. It measures whether it's a buy and	15 available?
16 a sell.	16 MR. SOHN: Objection to form.
17 Q. Okay. Now, you indicated earlier,	17 A. I haven't seen any specific
18 I thought, that buys at the offer, for example,	18 evidence regarding whether that information was
19 could have a tendency of pushing the price up.	19 publicly available. I know it was available to
20 MR. SOHN: Objection to form.	20 the parties about what they were doing. And
21 A. I'm not sure if I testified to	21 that's a flag to catch the effects of those
22 that. That might be the case.	22 variables -- of those -- of those transactions.
23 Q. Okay. You've seen literature to	23 Q. Well, isn't what your -- your
24 that effect, haven't you?	24 regression doing is trying to determine what
25 A. I may have, yes.	25 Badian's activity had on the price of Sedona in

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 the market?	2 A. Well, it was a general question,
3 A. That's the overall objective of	3 so I'm replying in a general sense.
4 the entire statistical analysis, is to figure	4 Q. So you're answering the question
5 out if there is an impact from any kind of	5 generally.
6 Rhino activity on the stock price.	6 Now, is it correct to say that to
7 Q. Well, isn't it important to	7 properly interpret the results of a regression
8 determine when you're modeling something	8 that you need to understand the design of the
9 whether that information was factored into the	9 study?
10 Q. Well, isn't it important to	10 A. To properly interpret the results
11 determine when you're modeling something	11 of the regression, yeah, you want to understand
12 whether that information was factored into the	12 the purpose of the analysis and the various
13 market by being publicly available?	13 different statistical analyses that are done to
14 MR. SOHN: Objection to form.	14 answer the question, which is the purpose of
15 A. I don't think it's important. I	15 the analysis.
16 don't think it's important to do that. I think	16 Q. Okay. And isn't it also true that
17 it's important to check -- look at your	17 different designs can result in different
18 analyses and make sure you're covering all your	18 answers?
19 bases by checking to see if there is any impact	19 MR. SOHN: Objection to form.
20 on the market through transfers of principal	20 A. Different designs may result in
21 transactions.	21 different answers.
22 Q. Well, isn't it correct to say that	22 Q. Okay. Now --
23 any analysis is only as good as the data on	23 A. That's what you're trying --
24 which it rests?	24 that's why you try to cover all your bases, to
25 MR. SOHN: Objection to form.	25 make sure that you covered all your bases.
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 Q. What do you mean by "accurate"?	2 Q. So, is it your position that the
3 A. Measuring what you think you're	3 data selected and the variables selected for
4 measuring accurately.	4 the independent variable has to be data that
5 Q. So, that, you want to make sure	5 can possibly have an impact on the dependent
6 that the data is data that is data that might	6 variable, this being the movement of the Sedona
7 have an impact on what you're measuring?	7 stock price in this case?
8 MR. SOHN: Objection to the form.	8 MR. SOHN: Objection to form.
9 A. You want to make sure that, A, the	9 A. Yeah. In this matter you want to
10 data is correct. That the data series you're	10 look at variables that potentially could have
11 using or the database you're using is --	11 an impact on Sedona's stock price, whether they
12 accurately reflects the data that you think	12 be buys, sells, transfers, principal. You want
13 it's reflecting.	13 to -- you want to look at all of that, so all
14 Q. Okay.	14 that could potentially have an effect on the
15 A. And, that, you want to use data	15 stock price.
16 that you think could potentially have an effect	16 Q. Could the validity of a regression
17 on the stock price, or variables that could	17 analysis be undermined by the use of
18 potentially have an effect on the stock	18 overinclusive data?
19 price.	19 A. I don't know what you mean by
20 Q. And is it fair to say that the	20 "overinclusive data."
21 design of the study determines the quality of	21 Q. Can a study be invalid because
22 the output of that study?	22 it's overinclusive?
23 A. In a very general sense.	23 A. I don't know what you mean by
24 Q. Is it -- what do you mean by "a	24 "overinclusive."
25 general sense"?	25 Q. Well, overinclusive in

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 relationship to the impact on the dependent</p> <p>3 variable that's being studied.</p> <p>4 A. Sorry, that doesn't help.</p> <p>5 Q. Remember my example of December of</p> <p>6 '09 and December of '07, my hypothetical?</p> <p>7 A. Barely.</p> <p>8 Q. Do you recall that I asked you</p> <p>9 whether or not what activity occurred in '07</p> <p>10 and what the -- what -- what the usefulness of</p> <p>11 that information would be in determining what</p> <p>12 someone did in trading stock in December of</p> <p>13 '09?</p> <p>14 A. I think you used different dates,</p> <p>15 but I remember the hypothetical, yes.</p> <p>16 Q. Okay. Well, I used the full date</p> <p>17 range. I'm just using the months now.</p> <p>18 The -- is it your position that</p> <p>19 you could select trading at any time during the</p> <p>20 period of time Sedona stock was trading to</p> <p>21 determine, for example, what happened in March</p> <p>22 of 2001?</p> <p>23 MR. SOHN: Objection to form.</p> <p>24 A. It's my position that there are</p> <p>25 two periods that you need to look at: One is</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 convertible debenture entered into?</p> <p>3 A. November of 2000.</p> <p>4 Q. Okay. And why did you include the</p> <p>5 period before the convertible debenture even</p> <p>6 existed --</p> <p>7 A. Because --</p> <p>8 Q. Excuse me.</p> <p>9 -- if what's being measured is</p> <p>10 activity that might be influenced by the</p> <p>11 existence of that convertible debenture?</p> <p>12 A. Because that includes a period in</p> <p>13 which Rhino was trading and in which Rhino had</p> <p>14 a previous FPS from Sedona. So I think it's</p> <p>15 very reasonable to want to understand what</p> <p>16 happened in that period, because that can tell</p> <p>17 you some things about what happens in the</p> <p>18 period after the issuance of the convertible G.</p> <p>19 Q. Well, let's take that period.</p> <p>20 Did you -- did you take a look to</p> <p>21 see what the trading patterns were during the</p> <p>22 period of time that was used to determine the</p> <p>23 price at which Badian could convert into Sedona</p> <p>24 stock from that preferred stock issuance?</p> <p>25 MR. SOHN: Objection to form.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 the entire period over which Rhino trades,</p> <p>3 because that's the entity -- entity that's the</p> <p>4 focus of interest. You want to understand what</p> <p>5 the data tells you about whatever price impacts</p> <p>6 there are from Rhino's trading over the entire</p> <p>7 time period that it trades.</p> <p>8 And then, there's a second period</p> <p>9 to look at, which is, I think, a reasonable</p> <p>10 period to look at, which concentrates -- it</p> <p>11 looks at a narrower period over which, you</p> <p>12 know, there's a -- there's a number of</p> <p>13 conversions. So I think those -- those are the</p> <p>14 two appropriate reasonable periods to look at.</p> <p>15 Q. Well, let's take the longer period</p> <p>16 of time. What was the time period? June of</p> <p>17 2000 through June of 2002?</p> <p>18 A. June of two -- June 26, 2000 to</p> <p>19 June 14, 2002.</p> <p>20 Q. Now, this case involves</p> <p>21 allegations of manipulating stock to gain an</p> <p>22 advantage in converting a debenture into --</p> <p>23 into that stock. Right?</p> <p>24 A. Right.</p> <p>25 Q. Okay. When -- when was the</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. From which preferred stock</p> <p>3 issuance?</p> <p>4 Q. The preferred stock issuance that</p> <p>5 existed, that it converted during that period</p> <p>6 of time.</p> <p>7 A. During what period of time?</p> <p>8 Q. Prior to November 22nd of 2000.</p> <p>9 A. I believe there was a conversion</p> <p>10 period in there. I'm not sure where it was.</p> <p>11 But if that is included in the date range that</p> <p>12 we looked at, then we looked at it.</p> <p>13 Q. Well, I mean, what I'm asking you</p> <p>14 is, did you take a look at the time period, the</p> <p>15 specific time period in which the conversion</p> <p>16 was priced and compare it with anything else?</p> <p>17 A. I think we have that data and I</p> <p>18 think I've looked at it, but I can't remember</p> <p>19 offhand what it tells you.</p> <p>20 Q. Is it in the report?</p> <p>21 A. No, it's not in the report.</p> <p>22 Q. Now, subsequent to May 31st, okay,</p> <p>23 were there any events that you know of that</p> <p>24 might have had an impact on Badian's trading</p> <p>25 strategy?</p>

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	MR. SOHN: 2001?	2	that's a disincentive?
3	MR. GUIDO: 2001.	3	MR. SOHN: Objection to form.
4	Q. After May 31st, 2001.	4	A. Well, I don't understand your
5	A. After May 31st, 2001.	5	question. If you can point me to somewhere in
6	Q. Uh-huh.	6	my report where you think I say that, I'd be
7	A. Yeah. Rhino still held a	7	happy to look at it.
8	significant position in the FPS. That didn't	8	Q. The -- you said that you read
9	go away until June of 2002. And, so, I think	9	Beloreshki's report, "The Frontiers of
10	that's legitimate to look at, too.	10	Convertible Financing." And that was one of
11	Q. Anybody ever show you an e-mail	11	the things that you based your opinion on is
12	from Andreas Badian to his brother that says	12	that you read the article.
13	they obviously knew what they were doing was	13	A. I said I had read the article,
14	wrong?	14	yes.
15	A. No.	15	Q. Okay. Well, do you recall that in
16	Q. Never saw that?	16	the article he indicated that one of the
17	A. Never saw that.	17	disincentives to market manipulation is that
18	Q. Did anyone ever tell you that, in	18	there's what's called a litigation contract
19	October of 2001, sedona refused to honor a	19	renegotiation.
20	conversion letter because it concluded that	20	A. I remember that discussion, but I
21	Badian was engaged in manipulation of its	21	don't remember the specifics of it. If you
22	stock?	22	want me to take a look at the article, I'd be
23	A. I may have. I can't recall if	23	happy to do so.
24	I've -- I can't recall if I've -- I don't think	24	Q. Why don't you take a look at
25	I've seen a document that tells me that. I	25	Exhibit No. 5.
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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	can't recall if I knew that at one point.	2	MR. SOHN: Five?
3	Q. But I think that when I asked you	3	MR. GUIDO: Five.
4	questions about, you know, as an economist, you	4	Q. And I direct your attention to
5	know, what are cost benefits, I think one of	5	page 7, item number 4.
6	the things you indicated was that a person	6	A. I see that.
7	might renege on their contractual obligations	7	Q. So one of the risks of -- that one
8	based on manipulative stock trading.	8	has to weigh is the litigation or contract
9	MR. SOHN: Objection to form.	9	renegotiation risk when one chooses to try and
10	A. No, I certainly didn't say that.	10	manipulate the stock price.
11	Q. What did you say?	11	MR. SOHN: Is that a question?
12	A. I said a person might renege on a	12	A. I don't see any reference to
13	contractual provision if the economics for that	13	manipulating a company's stock in here.
14	person works in a particular way. If a -- if a	14	Q. Does it talk about litigation
15	contractual provision says I have to pay a	15	risks with the issuer if the issuer is unhappy
16	million dollars to somebody and I don't have	16	about how the purchaser of a future price
17	the million dollars, well, I may have to -- I	17	security has acted?
18	may have to breach the contract.	18	MR. SOHN: Is that a question?
19	So, you know, there's something	19	A. It -- it does talk about
20	known as efficient breach. But I certainly	20	litigation risks in the third paragraph of that
21	didn't say what you said I said.	21	section.
22	Q. Well, I think that in your paper,	22	Q. Now let's turn to your -- the
23	in your expert report, you talk about how there	23	report that you signed. We'll start with page
24	are disincentives to market manipulation. Or	24	5. We haven't talked about the risk/return
25	am I wrong that you don't really think that	25	profile that you have here.

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	Do you have the report in front of	2	Is there a potential for the
3	you? Look at paragraph 18.	3	variables that you're looking at to have an
4	MR. SOHN: Mr. Guido, can we take	4	effect on Sedona's stock price?
5	a break at a convenient moment?	5	Q. Well, is the -- the weight of the
6	MR. GUIDO: Sure. Five-minute	6	variables, is that a relevant question to ask
7	break?	7	about whether or not the model is appropriately
8	MR. SOHN: Yes, thank you.	8	created?
9	MS. SCHECHTMAN: Yes.	9	A. I don't know what you mean by "the
10	THE VIDEOGRAPHER: Going off the	10	weight of the variables."
11	record at 3:21 p.m.	11	Q. Well, I mean you can -- you can
12	(A recess is taken.)	12	say trading or not trading. Okay? That's a
13	THE VIDEOGRAPHER: Going back on	13	potential to have an impact. Correct?
14	the record at 3:32 p.m.	14	A. I agree.
15	BY MR. GUIDO:	15	Q. Okay. And the -- the size of the
16	Q. If you were asked to evaluate the	16	trading or the frequency of the trading on a
17	models that were used for these regressions as	17	particular day could also be a relevant factor,
18	an expert, what questions would you ask as to	18	could it not?
19	whether or not the models were appropriate?	19	A. The side of the trade could be.
20	MR. SOHN: Objection to form.	20	Q. Anything else?
21	A. I would ask whether -- whether	21	A. Well, that's what I'm saying. You
22	there was a -- I would look to see whether	22	want to -- you want to look at variables -- you
23	there was a potential that the variables that	23	want to look at your measures and see if they
24	were being used as independent variables could	24	all have a potential to affect the stock price.
25	affect -- could be -- potentially affect	25	Q. Okay. Is the size of the trading
	Page 199		Page 201
1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	Sedona's stock price.	2	in relationship to the size of the market a
3	Q. Anything else?	3	variable that you would think to include in an
4	A. Could you repeat the question or	4	appropriately structured model?
5	have it read back?	5	A. That's a potential variable that
6	(Whereupon, the record is read	6	you should look at, and we did.
7	back.)	7	Q. So those are the -- those are the
8	A. I mean, I think that would be the	8	factors that you would look to to decide
9	basic question.	9	whether or not these models were appropriately
10	Q. Any others?	10	structured?
11	A. Well, I might have to -- there	11	MR. SOHN: Objection to the form.
12	might have -- there might be some with regards	12	A. Right. Are they independent
13	to the particular specifications of the	13	variables? Do they have a potential to affect
14	variables.	14	Sedona's stock price?
15	Q. I'm sorry, the --	15	Q. So one is whether selling exists
16	A. The particular specifications or	16	or doesn't exist, or buying exists or buying
17	combinations of the variables. But I think	17	doesn't exist. That's one.
18	that's the -- that's the main question from	18	Whether the -- whether size of the
19	a -- from a -- from -- if the question is with	19	sales or the buys have an impact?
20	regards to what -- what -- given that you think	20	A. Correct.
21	the regression analysis is appropriate, and in	21	Q. Whether the size in relationship
22	this setting, and what the -- what the proper	22	to other participants' behavior in the market
23	independent variables should be that you should	23	have an impact?
24	look at, then I think that's the main -- the	24	A. Can you say that again?
25	main answer.	25	Q. The size and relationship to other

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1 - STEPHEN D. PROWSE - 2 participants' activity in the marketplace. 3 A. Yes. Yes, that's -- that's a 4 potential variable. 5 Q. Now, when you did your analysis, 6 did the data include sales by Pond into the 7 market? 8 A. The data that we used came from 9 the account statements. So to the extent that 10 Rhino trades were executed through Pond, that 11 was included in the data. 12 Q. Meaning Rhino's sales to Pond were 13 reported in the data? 14 A. To the -- to the extent that 15 Rhino's trades were executed through -- by 16 Pond, that was included in the data. 17 Q. Well, is the data of Pond sales to 18 the market in the database? 19 A. The database is constructed to 20 look at data -- to look at Rhino's transactions 21 as reported in Rhino's account statements. 22 Q. Okay. 23 A. So all of the account statement 24 data is in our -- is in our database. 25 Q. Are you aware that the Rhino sales	1 - STEPHEN D. PROWSE - 2 That data was, I understand, 3 validated with NERA and edited at some point in 4 time by reference to documents Bates stamped 5 GOJO and RA, which I understand are account 6 statements and bank statements. 7 That database, that electronic 8 database, was a database that Mr. Beloreshki 9 took with him when he left NERA on CD and 10 stayed with him until he came to FTI. So that 11 was the data that we used when doing the 12 analysis on our report that is reported in 13 our -- in our report. 14 The -- subsequently, when we did 15 our report, we didn't have the source documents 16 at FTI that went into creating the electronic 17 database. But based on my conversations with 18 Mr. Beloreshki, I had a high confidence in the 19 accuracy and the precision of the data. 20 Subsequent to issuing our report, 21 we have now received all of the account 22 statements, all of the RA Bates document 23 statements, all of the GOJO Bates document 24 statements, all of the R statements, that we 25 have now since gone back and validated the
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1 - STEPHEN D. PROWSE - 2 in March and Badian sales to Refco were 3 executed by Pond? 4 MR. SOHN: Objection to form. 5 A. I can't recall the specifics. 6 That might be the case. 7 Q. But you don't know? 8 A. I don't know for certain without 9 looking at the data. 10 Q. Well, does the data that you 11 claimed to have looked at, does that include 12 sales by Pond? 13 A. To the extent that sales by Pond 14 came from Rhino transactions as reported in 15 Rhino's account statements, yes. 16 Q. Well, how was the data 17 constructed? 18 A. My understanding is the data was 19 constructed in the following manner, that -- 20 that we're using in this manner: Prior to 21 FTI's engagement in this matter, I understand 22 an electronic database was constructed by NERA 23 using account statements from accounts such as 24 Westminster, Amro, Refco, brokerages such as 25 Westminster and others.	1 - STEPHEN D. PROWSE - 2 electronic database that we used for the 3 analysis in our initial report. 4 And we made -- we found a number 5 of changes that we had to take. They were all 6 minor, I would say. Most of them had to do 7 with nonmarket transfers on dates outside, 8 dates either in 2000 or in 2002. There were a 9 couple of market transactions that were -- 10 there was one market transaction that was off 11 by a day, and I think there were a couple of 12 market transactions that were buys and sells on 13 the same days or subsequent days that were 14 actually canceled. 15 But after making -- but after 16 making those edits subsequent to issuing our 17 report, we -- we now have a database that we 18 think is as validated as it can be. And we've, 19 since issuing our report, rerun all our 20 statistical analyses that we did and nothing 21 changed from the results we -- our opinions 22 don't change. There may have been small 23 changes in the coefficients, but there were no 24 changes in anything of importance. 25 So our conclusions remain the same

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1 - STEPHEN D. PROWSE - 2 after we validated the data using the source 3 documents. 4 Q. So, you've gone back and you've 5 determined what the basis of the database was. 6 Last night I received, at eight 7 o'clock, a supplemental document production 8 that includes the documents that are Bates 9 stamped GOJO. 10 A. Yes. 11 Q. Is that the data -- is that the 12 universe of the account statements that you 13 used to verify the accuracy of the database? 14 A. Yes. We received last night those 15 documents, too. 16 Q. Okay. Let me -- let me just sort 17 of read through them, see whether or not 18 there's something missing in what I have based 19 on what you recall. 20 There was an account called 21 Cambois Finance of Westminster. Do you recall 22 that account? 23 A. I recall the name "Cambois." 24 Q. Okay. And was that one of the -- 25 one of the accounts with trades that you	1 - STEPHEN D. PROWSE - 2 Q. And what about an account BNC Bach 3 International and an entity called Dundee? 4 A. I believe that's in the database. 5 Q. Any other? 6 A. Not that I can remember off the 7 top of my head. 8 Q. This is all that I received. 9 A. Those -- all -- all those names 10 ring a bell with me. 11 Q. Okay. Well, did you look at any 12 Pond trade tickets? 13 A. We did not look at any Pond trade 14 tickets. 15 Q. And did you look at any Pond 16 account statements? 17 A. I'm not sure. I know Pond was a 18 broker for a lot of the transactions. So to 19 the extent that the trades, the Rhino trades, 20 went through Pond as a broker, then they would 21 be in the database. 22 Q. Are you sure of that? Because 23 when I looked at the columns in the database, 24 it doesn't include a column for Pond. 25 A. Well, my understanding is that
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1 - STEPHEN D. PROWSE - 2 included in your analysis? 3 A. I believe so, yes. 4 Q. Okay. Does that also apply to an 5 account at Westminster for an entity called 6 Roseworth Group? 7 A. I believe so, yes. 8 Q. Does that also include an account 9 for Amro International and an entity called 10 Refco Capital Markets? 11 A. I'm not certain about that now, 12 but I think so, but I'm not certain just 13 sitting here. 14 Q. What about a company called BNC 15 Bach International and a broker called Rampart? 16 A. Those -- those trades are 17 included, my understanding, yes. 18 Q. And what about an account in Amro 19 International and Westminster? 20 A. I understand that those data -- 21 that data is in the database. 22 Q. And what about an account BNC Bach 23 International and Canaccord? 24 A. I understand that's in the 25 database.	1 - STEPHEN D. PROWSE - 2 Pond was a -- a broker through which some of 3 Rhino's trades were made. And we -- my 4 understanding is we have the -- the entire 5 universe of Rhino trades regardless of who they 6 were actually trading through. 7 So to the extent that any Rhino 8 trades went through Pond in some manner, we 9 have those in our database. Now, if there are 10 Pond trades that are coming from some other 11 non-Rhino entity, then that -- that is not a 12 defendant in this matter, we wouldn't have 13 that. 14 Q. Well, I'm talking about 15 transactions that were transactions that were 16 initiated by Badian and that they were pre -- 17 they were initiated that Pond executed into the 18 market. 19 Are those transactions included in 20 your database? 21 A. Any Rhino transaction -- my 22 understanding is we have the universe of all 23 Rhino transactions. So if there is a Rhino 24 transaction that goes through Pond in some 25 manner, then that is in our database.

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 Q. Is every aspect of that reported	2 transactions in Sedona stock at Badian's
3 transaction included in your database?	3 request?
4 A. Well, I don't know what you mean	4 A. I just don't know one way or the
5 about "every aspect." We have -- I think -- I	5 other.
6 believe we have the price and I believe we have	6 Q. I'd like you to take a look at the
7 the number of shares and whether it was a buy	7 exhibit -- well, first of all, these are
8 or a sell. And I believe we have -- we	8 account statements based on the testimony of
9 obviously have the date of the trade. So if	9 Mr. Spinner of a proprietary account that he
10 that's what you mean, yes.	10 managed at Pond in which he executed trades on
11 Q. I want you to take a look at	11 behalf of Amro into the market.
12 documents that have been marked in this action	12 And my question is, have you ever
13 as Exhibits 86 through 90.	13 seen Exhibits 86 through 90?
14 MR. GUIDO: They're in reverse	14 A. I can't recall seeing them.
15 order, Josh, so switch them.	15 Q. Is any of the data in 86 through
16 Josh, can you make life easier for	16 90 included in your database?
17 me and pick a copy out of here for yourself?	17 A. Based on my understanding of the
18 One of the things I like is, in	18 data, if these are Rhino/Amro trades, if some
19 the index, to do a listing of the old exhibits	19 of these are Rhino and Amro trades, those
20 and where they first appeared in the	20 trades would be in our database. Because we
21 transcript.	21 have all the -- my understanding is we have all
22 BY MR. GUIDO:	22 the data for Rhino's transactions.
23 Q. While Mr. Sohn is pulling the	23 Q. Well, in your document production,
24 exhibits, why don't you take a look at the	24 I mean, look in your exhibit -- your exhibit --
25 packet.	25 I can't remember if it's two or three, where
Page 211	Page 213
1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 MR. SOHN: Can we take the others	2 you describe --
3 out? Can we take one more?	3 A. Three.
4 MR. GUIDO: I can only let you	4 Q. -- what it is you looked at.
5 have one.	5 A. Three.
6 MR. SOHN: Come on, Ken.	6 Q. Do you see any mention of these
7 MR. GUIDO: They're only	7 Pond trade tickets in these account statements?
8 accompanying you. I heard you introduce them.	8 A. No.
9 BY MR. GUIDO:	9 Q. So you didn't use them?
10 Q. Have you ever heard the name "Jake	10 A. No, I have already described how
11 Spinner"?	11 the data -- I understand the database to be
12 A. Yes.	12 constructed.
13 Q. Who is Jake Spinner?	13 Q. Well --
14 A. Who is Jake Spinner?	14 A. Five minutes ago.
15 Q. Yeah.	15 Q. I understand that. And we went
16 A. I believe he's a defendant in this	16 through the list of how the database was
17 matter.	17 constructed, did we not?
18 Q. Do you know what his role was	18 A. Went through the list? I'm not
19 in -- in this matter?	19 sure what list --
20 A. I believe he was at Pond Equities	20 MR. SOHN: Objection to form.
21 and his role is described in the Complaint. I	21 Q. Well, I asked you, based on what
22 can't give you the details, but I'd be happy to	22 was provided to me last night, which you
23 look at the Complaint, if you'd like.	23 indicated you probably received a copy of what
24 Q. Well, was he the broker at Refco	24 I received last night at eight o'clock, that --
25 that was responsible for the execution of the	25 that in that -- that is the universe of

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 information that went into your database.</p> <p>3 A. The GOJO documents are an input</p> <p>4 into the database, but my understanding is</p> <p>5 there are also RA Bates stamped documents and</p> <p>6 maybe some R stamped documents that are also</p> <p>7 inputs into the database. So it's a</p> <p>8 combination of those three documents which, in</p> <p>9 their entirety, my understanding is, covers all</p> <p>10 the account statements or trading activity of</p> <p>11 Rhino.</p> <p>12 Q. Well, in the Exhibits 86 through</p> <p>13 90, do you see any RA Bates stamp numbers on</p> <p>14 those?</p> <p>15 A. No.</p> <p>16 Q. But those documents have never</p> <p>17 been Bates stamped RA, have they?</p> <p>18 MR. SOHN: Objection.</p> <p>19 Q. To your knowledge.</p> <p>20 A. I don't know how I would know</p> <p>21 that.</p> <p>22 Q. Okay. So, are you aware that</p> <p>23 transactions were initiated by Mr. Badian by</p> <p>24 making calls to a man named Danny Graham, who</p> <p>25 then called a man named Cliff Abouf at Pond,</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 of that.</p> <p>3 Q. Now, in your exhibit, the -- you</p> <p>4 indicate that you looked at audit trail</p> <p>5 reports?</p> <p>6 A. Yes.</p> <p>7 Q. Did you notice anything out of the</p> <p>8 ordinary in the audit trail reports?</p> <p>9 A. I don't know what you mean by "out</p> <p>10 of the ordinary." They're thick reports about</p> <p>11 that thick. So, we looked at them. We noted</p> <p>12 what they were. We understood what they were</p> <p>13 based on the SEC's description of them in your</p> <p>14 response to interrogatories, but that's the</p> <p>15 extent of my knowledge.</p> <p>16 Q. Well, did you read the responses</p> <p>17 to the interrogatories?</p> <p>18 A. Yes.</p> <p>19 Q. And did you see in the responses</p> <p>20 to the interrogatories that described certain</p> <p>21 highlighting on those audit trail reports?</p> <p>22 A. Yes, blue highlighting, yellow</p> <p>23 highlighting, pink and orange, I believe.</p> <p>24 Something like that.</p> <p>25 Q. And did you see in those responses</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 and that Cliff Abouf then executed the trades</p> <p>3 into the market. And at the end of the day,</p> <p>4 Cliff Abouf and Danny Graham got together and</p> <p>5 they decided what number of shares Refco should</p> <p>6 sell to Pond to cover Pond's sales into the</p> <p>7 market.</p> <p>8 Are you aware of that?</p> <p>9 MR. SOHN: Objection to form.</p> <p>10 A. To the extent that's in the --</p> <p>11 that description is in the Complaint, I'm aware</p> <p>12 of that.</p> <p>13 Q. Other than in the Complaint?</p> <p>14 A. No.</p> <p>15 Q. Are you aware that the</p> <p>16 transactions that are reflected in Exhibit Nos.</p> <p>17 86 through 90 involving Sedona's shares were</p> <p>18 reported to the market?</p> <p>19 A. I don't know if they were reported</p> <p>20 to the market or not.</p> <p>21 Q. Are you aware that the Refco sales</p> <p>22 to Pond -- out of the Amro account to the Pond</p> <p>23 proprietary account managed by Mr. Spinner were</p> <p>24 reported to the market?</p> <p>25 A. I'm not aware one way or the other</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 to the interrogatories it explained the</p> <p>3 significance of those highlights?</p> <p>4 A. It did give a definition of what</p> <p>5 the highlights meant, yes.</p> <p>6 Q. And did you also, when you looked</p> <p>7 at that interrogatory response, see it included</p> <p>8 within the interrogatory responses was a</p> <p>9 description from FINRA of what the columns</p> <p>10 meant in the audit trail report?</p> <p>11 A. I believe I saw that.</p> <p>12 Q. Okay. Did you make an effort to</p> <p>13 determine which of the highlighted trades had</p> <p>14 been reported to the market?</p> <p>15 A. No, we did not do that.</p> <p>16 Q. Okay. So you don't know whether</p> <p>17 or not the Pond trades in Exhibit 86 through 90</p> <p>18 were reported to the market?</p> <p>19 A. We didn't do that analysis.</p> <p>20 Q. Okay. And you don't know whether</p> <p>21 the Refco to Pond transactions that were</p> <p>22 reflected in that -- in those audit trail</p> <p>23 reports were reported to the market?</p> <p>24 A. We didn't do that analysis.</p> <p>25 Q. Okay. Did you include in your</p>

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 analysis both the Pond trades into the market,	2 A. If all of Rhino's trades and
3 the sales into the market, and Refco's sales to	3 transactions were not in our database? Then
4 Pond in your analysis?	4 that's something that I'd want to investigate
5 A. We accounted -- in our database,	5 to see to what extent that database is not
6 we analyzed Rhino's trades; buys, sells and	6 capturing Rhino trading activity and when
7 other transactions. To the extent that they	7 was -- and for what period of time. And we'd
8 are covered by your descriptions, we -- they	8 obviously want to look at that and understand
9 are in our database.	9 why that's happening and try and -- try and
10 Q. Are you sure of that?	10 adjust for that.
11 A. I'm -- I mean, that's my	11 MR. GUIDO: I think one of the
12 understanding; that we have the universe of	12 exhibits that I showed Mr. Beloreshki is in the
13 Rhino's trades, regardless of who they went	13 originals. It's the 21A report.
14 through, and transactions. And to the extent	14 Could you show that to the witness,
15 that's true, then we have everything that Rhino	15 please?
16 did regardless of who it's through.	16 MR. SOHN: Exhibit 10.
17 Q. So you're saying in your database,	17 BY MR. GUIDO:
18 if I went back and looked at it, is that every	18 Q. In Exhibit 10, which was
19 trade, every transaction involved a sell by	19 previously called the 21A report, it was filed
20 Amro, out of an Amro-related account, that	20 by Rhino in this case. There's attached at the
21 every aspect of that transaction, if it was	21 end of it a schedule of transactions that I
22 reported to the market, would be included in	22 think is referred to as Exhibit D in that.
23 your database?	23 A. Yeah, I have it.
24 MR. SOHN: Objection to the form.	24 Q. Does that look familiar to the
25 A. Well, I'm not sure what you mean	25 electronic database that you indicated that you
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 by "every aspect" of that trade. If you mean	2 saw had been created in NERA?
3 the number of shares, whether it was a buy or a	3 MR. SOHN: Objection to the form.
4 sell, the day on which it occurred, yes, all	4 A. Well, obviously I can't testify as
5 that would be in the database.	5 to the numbers because I don't have the
6 Q. Well, assume this hypothetical:	6 electronic database to compare to, but some of
7 Assume that Andreas instructed Rhino to sell	7 the first -- the first four columns are similar
8 out of the Amro account stock to Pond,	8 in that that information is in our electronic
9 proprietary accounts that was run by Spinner.	9 database. The trade date, the buy/sell total
10 And he instructed Spinner to sell out of that	10 and the cumulative -- the quantity total and
11 account into the market the Sedona shares. And	11 the cumulative quantity total. Those are --
12 that he instructed both of those transactions	12 those are columns that are also in our
13 to be reported to the market. Just take that	13 electronic database.
14 as an assumption.	14 Q. And there are columns for
15 Would both of those transactions	15 different brokerage accounts also in your
16 be included in your database?	16 database. Isn't that correct?
17 MR. SOHN: Objection.	17 A. I believe that is correct. I'm
18 A. I believe so. I'd have to -- I	18 not entirely certain.
19 could check, but my assumption -- my	19 Q. Well --
20 understanding is that all Rhino trades and	20 A. I know there is a -- I know there
21 transactions are included in our database.	21 is a summary, a spreadsheet, that I'm familiar
22 Q. If they were not -- assume that	22 with that sums everything up for all accounts,
23 that hypothetical is true. If they were not,	23 brokerages, whatever.
24 would your database be inaccurate?	24 Q. I mean, that's the first three
25 MR. SOHN: Objection to form.	25 column in the spreadsheet, the aggregate data?

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 A. Right. And that's what I was	2 Prowse. Going back on the record at 4:23 p.m.
3 referring to. That's the data I'm familiar	3 BY MR. GUIDO:
4 with.	4 Q. I hand you the document I've had
5 Q. But with regard to the data, have	5 marked as BP-25.
6 you seen any spreadsheets that have columns for	6 Do you recognize that document?
7 transactions in the account at Pond Equities in	7 A. No, I don't.
8 which Jake Spinner had traded in?	8 Q. Do you recall that you prepared a
9 A. I just don't know.	9 set of notes reflecting your understanding of
10 Q. Well, did you see in the database	10 the Pet Quarters issues?
11 any equity that said "Pond Equities"?	11 MR. SOHN: Objection to form.
12 A. I can't remember seeing anything	12 A. I don't recall preparing any
13 that said "Pond." That doesn't mean it's not	13 notes, and I don't believe these are my notes.
14 there, but I can't remember seeing it. And	14 Q. Is there anybody at FTI with the
15 that doesn't -- that doesn't mean it might not	15 initials DS that worked on the Pet Quarters
16 be covered by something else. I just don't	16 matter?
17 know.	17 A. No. I don't -- I don't know what
18 Q. Well, I understand that, but I'm	18 DS stands for.
19 just asking if there's anything in the database	19 Q. Okay. Look under "Government
20 that you saw, anything that said "Pond	20 Theories." You see Number 2, "Manipulation
21 Equities" in the database. And you don't	21 pattern: (i) depress stock price by showing
22 recall seeing any?	22 store; (ii) submit conversion notice; (iii)
23 A. I don't recall.	23 engage in wash sales in order to enhance
24 Q. Well, in Exhibit No. 3, the	24 liquidity and artificially inflate the stock
25 documents you looked through, that also doesn't	25 price"? Do you see that?
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 make any mention to the account statements that	2 A. Yes.
3 I've shown you that have been marked as	3 Q. Now, does that control, to your
4 Exhibits 86 through 90, has it?	4 understanding, the Complaint in this case?
5 A. That's correct.	5 MR. SOHN: Objection to the form.
6 Q. And the list of GOJO account	6 A. I think that -- I think that could
7 statements which were provided to me at eight	7 be close, yeah.
8 o'clock last night, those also don't include	8 Q. Now, the -- now, did you do an
9 any reference to Pond Equities accounts, do	9 evaluation of wash sales to see whether or not
10 they?	10 they enhanced liquidity and artificially
11 A. I haven't gone through all the	11 inflated the Sedona stock price in your
12 GOJO documents, so I can't say one way or the	12 analysis?
13 other.	13 MR. SOHN: Objection to form.
14 MR. GUIDO: All right. Let's take	14 A. We did analyze the wash sales to
15 a break.	15 the -- because they were part of the data that
16 THE VIDEOGRAPHER: This concludes	16 we looked at.
17 Tape Number 3 in the videotaped deposition of	17 Q. Okay.
18 Dr. Stephen Prowse. Going off the record at	18 A. So --
19 4:09 p.m.	19 Q. Did you separate them out to
20 (A recess is taken.)	20 anyone?
21 (Whereupon, exhibit is received	21 MR. SOHN: Objection; asked and
22 and marked BP-25 for identification.)	22 answered.
23 THE VIDEOGRAPHER: This begins	23 A. We did not separate them out.
24 Tape Number 3 -- or, excuse me, Tape Number 4	24 They were part of the entire analysis.
25 in the videotaped deposition of Dr. Stephen	25 Q. Remember I showed you the

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 exhibit -- the rebuttal report from Pet	2 price movements of Sedona. But it -- but it
3 Quarters? And it had an exhibit at the end of	3 wasn't just the characteristics of the
4 it. It did an analysis of those, of the trades	4 security. It was also the characteristics of
5 in Pet Quarters.	5 Sedona that made this an optimal trading
6 A. Some trades in Pet Quarters,	6 strategy -- or economically rational optimal
7 correct.	7 trading strategy.
8 Q. Some trades. The Westminster/	8 Q. But just talking about the
9 Amro-related accounts and the Refco/Amro-	9 debenture in the agreement itself.
10 related accounts. Remember that?	10 So that one of them was that it
11 A. I'm not sure they were all	11 had a convert -- a floating conversion price.
12 Westminster/Refco. I think some of them might	12 A. Correct.
13 have been, but not all of them.	13 Q. That was one of the factors --
14 Q. But they were trades between	14 A. Correct.
15 related entities?	15 Q. -- to be considered?
16 A. I think that's right.	16 A. Right.
17 Q. And you recall that you did an	17 Q. And that it was a debt instrument
18 analysis to determine whether or not they	18 in which Sedona's financial condition presented
19 are -- how close they were to the offer or they	19 a risk. Is that fair?
20 bid or somewhere in between?	20 A. That's correct. The fact that it
21 A. Correct.	21 was a debt instrument; the fact that it was a
22 Q. And did you do such an analysis	22 risky security. For a variety of reasons. The
23 with regard to the Sedona matter?	23 fact that there was a floating conversion
24 A. We did not do that analysis in	24 price. Those were the -- there was a lockup
25 this matter.	25 period. Those were the characteristics --
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 Q. Now, this -- I want to go page 5	2 Q. What's a lockup period?
3 where you talk of the risk/return profile and	3 A. A period over which after
4 what a rational trading strategy is.	4 issuing -- after issuance of the FPS, the
5 MR. SOHN: Page 5 of Exhibit 4.	5 investor is not allowed to convert.
6 Correct?	6 Q. Not allowed to convert.
7 MR. GUIDO: Page 5 of Exhibit 4.	7 And there was a lockup period
8 MR. SOHN: Thank you.	8 here?
9 BY MR. GUIDO:	9 A. Yeah.
10 Q. The -- in paragraph 18, you talk	10 Q. What did that -- what was the
11 about what's an economically rational and	11 language of that lockup period?
12 beneficial trading strategy for holders of such	12 A. I can't remember the lockup period
13 debentures; i.e., the Sedona November -- I	13 language, but -- sitting here.
14 think it's November 22nd, 2000 debenture.	14 Q. What was the lockup period?
15 And what is your understanding of	15 A. I think it was three months.
16 the provisions of that debenture that were	16 Q. What time period to what time
17 relevant for your determination of whether or	17 period?
18 not Badian had engaged in an economically	18 A. November 22nd, I believe, to March
19 rational and beneficial trading strategy?	19 22nd, I believe, of 2001.
20 MR. SOHN: Objection to form.	20 Q. Was one of the other risks of the
21 A. Well, there were -- the provisions	21 instrument that it had a provision in it that
22 that made it an FPS, for example; that there	22 prohibited short sales?
23 would be a conversion price -- that there would	23 A. Well, I wouldn't say that was a
24 be a right to convert based on a floating	24 risk. That was a provision that increased the
25 conversion price that was linked to the stock	25 riskiness of the -- of the security.

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 Q. That was a lockup period, wasn't	2 MR. SOHN: Objection to form.
3 it? I mean, you could interpret it that way,	3 A. Yeah.
4 couldn't you?	4 Q. Well, it says "reduce their
5 A. I interpret a lockup period	5 overall long position in the underlying equity
6 meaning that's the period over which your --	6 whenever possible." Okay?
7 you can't convert. The company won't honor a	7 A. Correct.
8 conversion notice.	8 Q. And then "extend the period in
9 Q. I mean, it's -- I mean, in future	9 which such positions were unwound."
10 price securities, is one of the issues that is	10 I mean, why are those -- I mean,
11 discussed in the negotiations the limitations	11 if you say whenever possible, doesn't that mean
12 on the ability to convert?	12 as soon as possible?
13 A. Absolutely. That's one of many	13 A. Yes.
14 different contract provisions that are	14 Q. And then --
15 negotiated between the parties, including the	15 A. As soon as -- as soon as -- start
16 discount; whether there is a lockup period and	16 as soon as possible and unwind -- and unwind
17 the length of it; obviously the amounts.	17 your long position in the FPS or the underlying
18 The -- various other contractual provisions are	18 equity by shorting the stock and -- until the
19 all negotiated.	19 conversion period and then convert.
20 Q. Floors under conversion prices?	20 Q. I'm sorry. I'm just looking at
21 A. You can have floors, you can have	21 this. I'm trying to understand what this
22 caps. Yes.	22 sentence means, not what you just said.
23 Q. And do those affect the interest	23 A. Well, I just explained what it
24 rate that a purchaser would request in its	24 said.
25 negotiations?	25 Q. Well, I'm sorry, maybe I missed
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 A. They all go into -- all those	2 it.
3 factors go into the agreed upon -- all the	3 You start as soon as possible.
4 factors are agreed upon simultaneously and one	4 Reduce your overall long position in the
5 will affect the other. So you may get a	5 underlying equity whenever possible. That
6 longer -- a longer lockup period and a higher	6 means you start unwinding as soon as possible.
7 discount or -- depending upon the preferences	7 Okay?
8 of the parties. Just something like that.	8 Then it says "to extend the
9 Q. Now, you indicate that Badian's	9 period over which such positions were
10 trading strategies and the way he unwound	10 unwound."
11 Amro's positions in Sedona's stock was	11 What does that mean?
12 consistent with a trading strategy that you	12 A. No, I would say it differently. I
13 refer to in paragraph 18.	13 would say whenever you see a chance -- whenever
14 Now, what -- what was the trading	14 there is a chance, an optimal trading -- the
15 strategy that you're referring to?	15 first clause to me means whenever there is a
16 MR. SOHN: Objection to the form.	16 chance to un -- to unwind your position, unwind
17 A. The trading strategy that's	17 your long position, you take it.
18 referred to in the previous sentence. To	18 And, furthermore, you -- and this
19 reduce -- "seek to reduce their overall long	19 is the second clause. You start that process
20 position in the underlying equity whenever	20 as early as possible, because as soon as you
21 possible and to" the extent -- "and to extend	21 invest in the FPS, you're at risk.
22 the period over which such positions were	22 Q. Well, if you have an FPS that
23 unwound."	23 is -- the price is a floating price based on
24 Q. Can -- are those -- those two	24 stock price and you're buying at a discount --
25 statements consistent?	25 in this case I think it's 85 cents on the

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 dollar. Right?	2 Was that a rational economic
3 A. (Indicating.)	3 decision on their part?
4 Q. What's the magnitude of the risk	4 MR. SOHN: Objection. It's an
5 when you're holding the -- holding the	5 incomplete hypothetical.
6 debenture prior to conversion?	6 A. It may or may not have been. I
7 A. Well, that's where the nature of	7 don't know if they were aware what they were --
8 the company comes in. The magnitude of the	8 what they were entering into in terms of a
9 risk is -- consists of a number of risks:	9 nonshort provision. It may or may not have
10 credit risk, default risk, liquidity risk,	10 been an economically rational decision.
11 delisting risk. And the size of those risks	11 But once that decision's made and
12 depends on the riskiness of the company.	12 you are in a position where you're in an FPS,
13 This was an extremely risky	13 you're an extremely -- you're holding extremely
14 company. Highly volatile stock price, very	14 risky security. And a way to hedge that risk
15 poor operating performance, unable to raise	15 is to short and cover yourself.
16 money in any other way than through an FPS.	16 Q. Well, if it's a floating price
17 Periods of time over which the stock price	17 conversion, how great is the risk if the price
18 could easily fall 90 percent.	18 goes down? Don't you just get more stock
19 This was a -- this was a company	19 that's equal to the amount that you tendered
20 that presented high credit risk, high default	20 for the conversion?
21 risk, high liquidity risk and high delist --	21 A. That's one protection, but it's
22 delisting risk. And all that together meant	22 not a complete protection. You've got -- as
23 that your holdings in the FPS were extremely	23 I've said, as I said five minutes ago, you've
24 risky right from the get-go.	24 got credit risk, you've got default risk, you
25 And, so, you would want to cover	25 have delisting risk, you have liquidity risk,
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 yourself for that.	2 all of which can result in a decline of the FPS
3 Q. Did Amro extend the convertible	3 and a decline in the value of the FPS and a
4 debenture?	4 decline in the value of the stock or your
5 A. I believe it did.	5 ability to get cash out of the stock when you
6 Q. When did it do that?	6 eventually get it.
7 A. I don't know the date.	7 Q. Was all of that information
8 Q. When did it begin to negotiate	8 available to Badian and Rhino and Amro at the
9 that?	9 time that they agreed to extend the convertible
10 A. I don't know the date.	10 debenture?
11 Q. Did Amro and Rhino and Badian sign	11 MR. SOHN: Objection to form.
12 a nondisclosure agreement to look at the	12 A. I would assume that both Sedona
13 financials of Sedona when they did so?	13 and Rhino are sophisticated parties. And when
14 A. I'm not aware of whether they did	14 they enter into a contract, they understand the
15 or didn't.	15 risks that they are entering into. And -- but
16 Q. So you don't know?	16 once you have entered into that contract, those
17 A. I don't know.	17 risks are there and you want to hedge them to
18 Q. Well, assume that they did, okay,	18 the -- to the greatest extent you can.
19 for purposes of giving your opinions. And they	19 Q. Now, isn't -- isn't there a risk
20 decided to extend the term after they had seen	20 in holding Sedona stock long?
21 the financials on a confidential basis. And	21 MR. SOHN: When?
22 they extended the debenture which had a	22 MR. GUIDO: At any point in time.
23 provision in it which prohibited them from	23 A. Sure, there's a risk with holding
24 shorting the stock prior to submitting a	24 any -- any kind of financial instrument. It's
25 conversion letter.	25 just a question of whether it's a -- it's a

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 question of the degree.	2 quickly -- as soon as you can without having
3 Q. The degree. Okay.	3 any impact on the market. Slowly unwind your
4 When Sedona converted -- I mean	4 long position till you get to a point at which
5 when Amro converted the stock in their	5 you can convert. Then make a decision about
6 conversions in the spring of 2001, did it end	6 whether you want to convert or not, depending
7 up long, the stock?	7 upon how much you've been able to cover
8 A. It ended up long, the stock, but	8 yourself.
9 not by much and for a short period of time.	9 And if you decide to convert, then
10 Q. Well, what do you mean by "not by	10 you have to decide how much you're going to
11 much"?	11 convert and that would depend on how much
12 A. Not by much. I mean, at most I	12 you've been able to short. And then start
13 think a hundred -- a couple hundred thousand	13 again depending on how much you have left to go
14 shares, maybe, if that.	14 in terms of your conversion.
15 Q. Really?	15 Q. Well, when did they -- when did
16 A. For short periods.	16 they start shorting the stock there?
17 Q. Really?	17 A. You mean after November 22nd?
18 A. Yeah, really.	18 Q. Uh-huh.
19 Q. Not 814,000?	19 A. I mean, I would have to look at
20 A. Nowhere close to that.	20 the data to tell you the day when they started,
21 Q. Nowhere close to that?	21 but I can't tell you sitting here.
22 A. No.	22 Q. Have you ever seen any of the
23 Q. Where do you get that information?	23 reports that Danny Graham sent to Andreas
24 A. From our database that you have.	24 Badian on the short transactions in the
25 Q. Well, you have the data -- you	25 Refco/Amro account?
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 have the aggregate data, don't you, on that	2 A. No, I don't believe I have.
3 Exhibit 14, or am I wrong in what's in Exhibit	3 Q. I'd like you to take a look at a
4 14? No, I'm sorry, it's not in Exhibit 14.	4 document that's been previously marked as
5 But in your database it shows that	5 Exhibit No. 57. And I'd like you to turn to
6 -- in the database it shows --	6 the page -- as you can see, this is an e-mail
7 A. Just the accumulated position in	7 on Wednesday, March 28th, from Danny Graham to
8 terms of shares on a daily basis.	8 Andreas Badian. It's called a Refco
9 Q. On a daily basis.	9 spreadsheet.
10 And, so, that, after the	10 Look at the page SDNA, about the
11 conversions, that Sedona was not long the stock	11 third or fourth in. I guess it's not the third
12 more than a few hundred thousand shares?	12 or fourth.
13 A. Well, I want to be careful about	13 Are you at that page?
14 the time period, but -- and there may have been	14 A. Yes.
15 a brief period where it was a little more than	15 Q. This is a summary of the
16 that, but I don't believe it was ever close to	16 transactions in the Refco account in Sedona --
17 being 860,000 shares long.	17 I mean in the Amro account. It's a -- I mean
18 Q. Okay. So your view is that they	18 the Refco account for Amro in Sedona stock.
19 should short the stock as much as possible and	19 And it indicates that the short selling
20 then they should convert and get rid of the	20 started, that's involved here, on February
21 stock that they have as soon as possible?	21 21st. That is three months after the
22 A. I would phrase it differently. I	22 convertible debenture was even entered, isn't
23 would phrase it that what they should do, or	23 it?
24 what an optimal strategy would be for holding	24 A. Yes.
25 an FPS, is to start hedging yourself as	25 Q. Is that what you call as soon as

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1 - STEPHEN D. PROWSE - 2 possible? 3 A. Well, I don't know if this is the 4 sum total of Rhino transactions. So, I just 5 don't know whether this is representing all of 6 Rhino's transactions. 7 Q. So, Rhino or Amro could have been 8 selling through other accounts other than the 9 Refco account? 10 A. They could have been. 11 Q. Take a look at Exhibit No. 47 12 again. 13 Do you see that? 14 MR. SOHN: Which one? 15 MR. GUIDO: I think it was -- 16 MR. SCHECHTMAN: This one? 17 MR. GUIDO: Excuse me. It was the 18 21A report. 19 THE WITNESS: This one? 20 MR. GUIDO: What's the exhibit 21 number? 22 BY MR. GUIDO: 23 Q. Does that reflect aggregate 24 transactions in Sedona stock by Amro-related 25 activities?	1 - STEPHEN D. PROWSE - 2 to answer your question here. 3 Q. Is it your understanding that 4 Badian, acting on behalf of Amro, shorted the 5 stock of Sedona prior to February 21st of 6 2001? 7 A. As I said before, I can't give you 8 a date without looking at the data for the 9 cumulative holdings which are in our -- in our 10 work sheets. And the date just doesn't come to 11 mind at which Rhino first was in a short 12 position after issuance of the November 22nd 13 FPS. 14 Q. Now, assuming that you're correct, 15 that that's what rational strategy in the 16 shorts did occur at an earlier point in time, 17 is it also an economically rational strategy to 18 short the stock as much as possible, convert at 19 a low price, and by pushing the price down 20 using whatever market strength that Badian had, 21 converting the larger number of shares and 22 then, using NASDAQ trades to push up the market 23 price and unload those additional shares at the 24 higher price? 25 MR. SOHN: Objection to form.
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1 - STEPHEN D. PROWSE - 2 A. Does what -- 3 MR. SOHN: Objection to form. 4 A. Does what reflect? 5 Q. The Schedule D on Exhibit No. 10, 6 which is the earlier Exhibit No. 47. 7 MR. SOHN: Does it what? 8 Q. It's Exhibit D, or Schedule D, on 9 Exhibit No. 10. 10 MR. SOHN: Right. And what's the 11 question? 12 Q. Does that reflect the aggregate 13 transactions in Sedona stock during the time 14 period after they were entering into the 15 convertible debenture? 16 MR. SOHN: Are you asking 17 Dr. Prowse if that's accurate or if it reports 18 what it purports to report? 19 BY MR. GUIDO: 20 Q. Does it purport? 21 A. I don't even know what it 22 purports. I haven't read this document. It's 23 a very long document with 23 pages and a large 24 number of spreadsheets. So I don't know what 25 it's supposed to purport. So I don't know how	1 - STEPHEN D. PROWSE - 2 A. Well, number one, that's a 3 strategy that increases your risks in a number 4 of aspects. And, number two, that's not what 5 our empirical analysis finds, that there was no 6 price impact one way or the other of Rhino's 7 trades. And, so, with regards to number one, 8 -- 9 Q. My -- 10 A. -- the optimal strategy -- 11 Q. Excuse me. I'm sorry for 12 interrupting, but I'm not asking what they did 13 here. I asked you a hypothetical. 14 I said isn't it a rational 15 strategy, economically rational, if you have 16 the ability to do it -- to short stock at a 17 higher price, push it down and convert at a 18 lower price, and then to use mechanisms such as 19 wash trades to push it up to give you the 20 excess stock at a higher price? Isn't that an 21 economically rational approach? 22 MR. SOHN: Objection to form. 23 A. I think a more economically 24 rational approach is just to short the stock 25 without any intent to push it down, cover

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1 - STEPHEN D. PROWSE - 2 yourself. When you get to a point that you can 3 convert, convert, and continue to do that all 4 the way through to the end of the FPS. That 5 avoids risks associated with manipulating the 6 stock. 7 Q. Well, let me give you a 8 hypothetical. Okay? And that is the stock is 9 trading at a buck. And, so, I short a million 10 shares at a dollar. And I have the ability to 11 push it down to 50 cents. And I push it down 12 to 50 cents. And I convert at a 50-cent price. 13 And I get my million shares -- I get the 14 million shares that I sold at 50 cents and I 15 get another million shares at 50 cents. And 16 then I enter into wash sales and I push the 17 price back up to a buck and I unload it. 18 Don't I make much more money than 19 I had sold -- than if I had sold the million 20 shares and converted the million shares after, 21 at a buck? 22 A. I guess in your hypothetical, to 23 the extent I understand it, you've set it up 24 that way, yes. It's almost tautologic. 25 Q. No, I understand that. But isn't	1 - STEPHEN D. PROWSE - 2 What's the question? 3 MR. GUIDO: I'm sorry. 4 MR. SCHECHTMAN: Wait. Ken, can 5 we just get the question read back? 6 MR. GUIDO: Yes. 7 MR. SCHECHTMAN: Thank you. 8 (Whereupon, the record is read 9 back.) 10 MR. GUIDO: Are we waiting for 11 something? 12 MR. SOHN: She didn't -- she 13 didn't really have what the question was. 14 MS. SCHECHTMAN: And it didn't 15 sound like a question. 16 MR. SOHN: It sounded even less 17 like a question than it did the first time. 18 MR. GUIDO: Let me ask you a 19 question, or let me ask you the question with 20 Ms. Schechtman's permission. 21 BY MR. GUIDO: 22 Q. And that is the -- are you telling 23 me, or us, that there is no rational 24 economic -- there's no economically rational 25 reason to engage in market manipulation?
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1 - STEPHEN D. PROWSE - 2 it -- isn't that also a feasible strategy? 3 A. I don't know if it's a feasible 4 strategy or not. It depends on the stock, it 5 depends on the entity, it depends on the risks 6 of the security, it depends on the risks of the 7 company. It depends on the risks of 8 manipulating -- actually manipulating the 9 stock, and depends on your ability to do that. 10 Q. Well, there are a lot of 11 uncertainties in life, including your -- your 12 hypothetical of the appropriate hedging 13 strategy, aren't there? 14 MR. SOHN: Objection. 15 A. That's not my hypothetical. 16 That's my opinion. 17 Q. Okay. 18 A. It's your hypothetical of the -- 19 Q. It's my hypothetical. And your 20 opinion is also a hypothetical. And that is 21 that you basically short the stock and then you 22 convert. Right? 23 A. That's not a hypothetical. 24 MR. SOHN: That's a question? 25 MR. SCHECHTMAN: Wait. Stop.	1 - STEPHEN D. PROWSE - 2 A. What I'm telling you is that, 3 hypothetically, I can see that there would be 4 economic incentives to engage in manipulation. 5 Manipulation happens. It just doesn't happen 6 in this case. 7 There was a -- there was an 8 economically rational strategy for trading the 9 equity of Sedona based on the riskiness of the 10 FPS, which was largely mirrored by Rhino's 11 strategy, and there was no empirical evidence 12 to support Rhino having -- having any impact on 13 the price. And Sedona was a highly risky 14 company whose stock price could go up, was 15 extremely volatile. And that contributed to 16 the optimality of the hedging strategy and also 17 contributed to the riskiness of the stock and 18 why it would go down. 19 Q. Well, let me read you something. 20 And that is, "Contract-based and trade-based 21 manipulation is neither impossible nor 22 self-deterring. Possible economic models 23 indicate that manipulation can be profitable." 24 Manipulation -- "Manipulative trading may or 25 may not be common, but it is possible and

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 tempting in a variety of significant and common</p> <p>3 situations."</p> <p>4 Do you agree or disagree with that</p> <p>5 statement?</p> <p>6 A. I think that's what I largely</p> <p>7 said, that there could be economic situations</p> <p>8 where manipulation works, but it just didn't</p> <p>9 work in this case. It didn't happen in this</p> <p>10 case for the reasons I just gave.</p> <p>11 Q. And you said it was based on</p> <p>12 empirical evidence?</p> <p>13 A. It's based on an analysis of the</p> <p>14 optimal trading strategy; it was based on an</p> <p>15 analysis of the risks Sedona presented to</p> <p>16 investors; and it was based on empirical</p> <p>17 analysis. Yes.</p> <p>18 Q. Was it based on what the people</p> <p>19 who were engaged in the activity themselves</p> <p>20 thought they were doing?</p> <p>21 MR. SOHN: Objection to form.</p> <p>22 A. It was based on the three inputs</p> <p>23 that I -- the three pieces of analysis that I</p> <p>24 talked about.</p> <p>25 Q. Okay. Did you consider at all</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. No.</p> <p>3 Q. The numbers, as far as you're</p> <p>4 concerned, are the controlling variable?</p> <p>5 A. No. My report is the -- my report</p> <p>6 is my report and all the elements of my</p> <p>7 report --</p> <p>8 Q. Okay.</p> <p>9 A. -- that go into that.</p> <p>10 Q. Okay. But I'm giving you another</p> <p>11 variable that you didn't consider.</p> <p>12 A. Correct.</p> <p>13 Q. And that is that the people who</p> <p>14 engaged in the activity concluded that they had</p> <p>15 pushed the price down to 75 cents at Badian's</p> <p>16 direction.</p> <p>17 MR. SOHN: Objection.</p> <p>18 Q. Does that affect your conclusions</p> <p>19 in your report?</p> <p>20 MR. SOHN: Objection to form.</p> <p>21 A. The evidence doesn't support that</p> <p>22 notion.</p> <p>23 Q. Well, let's go -- let's talk about</p> <p>24 the regressions now. You did five regressions</p> <p>25 on the March 1st to May 31st transactions. And</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 what the people who were executing the</p> <p>3 transactions thought they were doing?</p> <p>4 A. We didn't get -- we didn't get</p> <p>5 into that. We weren't asked to look at that.</p> <p>6 Q. So you've never seen or</p> <p>7 listened -- seen transcripts or -- of</p> <p>8 audiotapes or heard audiotapes of what</p> <p>9 Mr. Badian was saying or that people who were</p> <p>10 executing trades on his behalf were saying</p> <p>11 about what he was doing?</p> <p>12 A. I have not.</p> <p>13 Q. Would your opinion be affected if</p> <p>14 you learned that the people who had executed</p> <p>15 the trades had concluded that Badian had pushed</p> <p>16 the price down in order to increase his</p> <p>17 conversion, the number of shares to get on</p> <p>18 conversion?</p> <p>19 MR. SOHN: Objection to form.</p> <p>20 A. That's not what the data I've</p> <p>21 analyzed tells me. That's not what I've</p> <p>22 concluded in my report. So that wouldn't</p> <p>23 change my opinion.</p> <p>24 Q. So it wouldn't change your</p> <p>25 opinion?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 then there's another one that you don't list,</p> <p>3 and that is net daily trading excluding the</p> <p>4 impact to the NASDAQ, which you don't even</p> <p>5 mention.</p> <p>6 A. That's incorrect.</p> <p>7 Q. Well, I -- I don't see a piece of</p> <p>8 paper that says you did it. I had to have</p> <p>9 somebody go back and reconstruct the model to</p> <p>10 determine it. There's not a piece of paper</p> <p>11 that you've produced in this case that said you</p> <p>12 did that last regression.</p> <p>13 A. Which last regression?</p> <p>14 Q. The regression of net daily</p> <p>15 trading absent the impact of the NASDAQ. There</p> <p>16 is not a piece of paper that says you did that</p> <p>17 regression anywhere in what you've produced.</p> <p>18 A. Well, I understand -- I understand</p> <p>19 that we did that regression. I understand we</p> <p>20 did nine regressions, not five.</p> <p>21 Q. Okay.</p> <p>22 A. Nine regressions for each period.</p> <p>23 Q. Okay. Well, I'm sticking to the</p> <p>24 March 1st to May 31st -- March 1st to May 31st</p> <p>25 time period right now. Okay?</p>

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	And the -- the question is, you	2	A. And that is --
3	came up -- you did what you call nine	3	MR. SOHN: Mr. Guido, please let
4	regressions, and that three of them show a	4	the witness finish his answer.
5	significant correlation, although one of them	5	A. That is inconsistent with the --
6	is weak. It's a 7.08, one which is net trading	6	with the information you just gave me. And
7	as a percentage of total volume.	7	it's also consistent with your experts'
8	One of them is net daily trading	8	analysis. Your experts ran our regressions for
9	factoring out the impact of the NASDAQ. And	9	another time period, yet another time period.
10	the third is net daily trading ignoring the	10	And in their time period, they found no -- even
11	impact of the NASDAQ, which you, in another	11	on a stand-alone basis no statistically
12	correlation, have indicated during this time	12	significant -- a "P" value of less than 5
13	period is statistically insignificant in terms	13	percent.
14	of its impact.	14	Q. All right. Let's talk about the
15	So you've got three regressions	15	massive evidence. Okay? One of them is
16	that show a statistically significant	16	NASDAQ. Right? The background. I'm taking --
17	relationship between Badian's trading activity	17	I'm using your report.
18	and the stock price of Sedona.	18	A. Okay. I'm not sure what
19	Now, why isn't that consistent	19	particular part of my report you're referring
20	with the testimony that I've just told you	20	to.
21	exists in this record that the people that	21	Q. Well, I mean, you're talking that
22	engaged in the trading activity on behalf of	22	you did a lot of analysis and there's a massive
23	Badian concluded that Badian had pushed the	23	amount of amount. One of them is what NASDAQ
24	price down to 75 cents?	24	did. The other is what the peer group did.
25	MR. SOHN: Objection to form.	25	The third is the events, the company-specific
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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	A. For a variety of reasons. First	2	events.
3	off, none of the relationships that you've just	3	A. Actually I was talking about --
4	described are properly considered to be	4	Q. Anything else?
5	significant when -- when considered in the	5	A. -- the actual statistical
6	context of the battery of tests we ran.	6	analysis. But if -- but, certainly, that's
7	We ran numerous parametric	7	true.
8	analysis, nonparametric analysis. We ran 18	8	Q. Okay.
9	regressions. It doesn't surprise me at all	9	A. That's broadening out --
10	that I would get a spurious correlation in two	10	Q. And you found that NASDAQ --
11	of them. It just doesn't. That's what --	11	(Indiscernible cross-talk; Reporter
12	that's what to be expected from statistics.	12	requests one speaker at a time.)
13	Controlling for that spurious	13	A. Broadening it out to Section 3,
14	correlation tells you that you cannot reject	14	yes, you're correct, those other factors also
15	the hypothesis of no impact when you have a	15	play a role.
16	mass of results that tell you where the	16	Q. Okay. And you testified that with
17	piece -- where the "P" value is greater than 5	17	NASDAQ, March -- March 1st to May 31st, there's
18	percent, and only two that tell you the "P"	18	no statistical correlation between the NASDAQ
19	value is less than 5 percent.	19	and Sedona's price. Correct?
20	Q. Let's --	20	A. Correct, that's what the
21	A. So there is --	21	regression showed.
22	MR. SOHN: Mr. Guido.	22	Q. All right. And with regard to the
23	A. There's a mass of evidence that	23	peer group, you didn't do it, because you
24	shows no impact.	24	didn't have the data to do it. Right?
25	Q. Okay. Mass of evidence --	25	A. I'm not sure if we didn't have the

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1 - STEPHEN D. PROWSE - 2 data. I'm not sure that's the exact reason, 3 but we didn't do it. 4 Q. But you didn't do it. 5 A. We didn't -- we didn't put it in 6 the regressions. We looked at it and compared 7 Sedona's stock price -- 8 Q. No, I understand. You didn't -- 9 A. -- decline -- 10 MR. SOHN: Mr. Guido. 11 A. -- with the average decline of the 12 peer group, found that it was totally in line. 13 Q. You didn't do a statistical 14 analysis comparing -- a regression analysis 15 comparing the peer group performance with 16 Sedona's stock performance, did you? 17 A. We didn't do a regression 18 analysis -- 19 Q. Thank you. 20 A. -- with the peer index. We did 21 another type of analysis. 22 Q. Thank you. 23 And you didn't do an event study 24 on the various events that you cite in your 25 report: The issuance of 10-Ks, the purchases	1 - STEPHEN D. PROWSE - 2 Isn't that correct? 3 A. That's exactly correct. 4 Q. Okay. 5 A. There was no impact of the -- of 6 the trans -- of the transactions. And there 7 was also no impact of the trades. 8 Q. Now, so, then you've got -- you 9 put those aside and you've got left the 10 statistical analyses that you did on these 11 three situations: One is that daily trades as 12 a percentage of volume; net daily trades 13 including factoring out the impact of NASDAQ; 14 and, third, net daily trades of -- for not -- 15 not including the impact of the NASDAQ. 16 Correct? 17 A. As well as the other regressions 18 we ran. 19 Q. Okay. The other regressions. 20 And the other regressions included 21 regressions in which you put information that 22 you have testified as far as you know was not 23 public information? 24 MR. SOHN: Objection. 25 Q. Including transfers and -- and
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1 - STEPHEN D. PROWSE - 2 of stock. You didn't do any event studies to 3 indicate whether those in isolation had an 4 impact on Sedona's stock price performance. 5 A. That's incorrect, as we talked 6 about a couple hours ago. And we went into 7 that in detail a couple hours ago. That's just 8 incorrect. 9 Q. Where is the event study for each 10 of those events? I didn't see it anywhere in 11 your report. 12 A. You mentioned an event study for 13 stock purchases, and I -- we went through this 14 two or three hours ago. I told you that we had 15 indicator variables in our regressions for 16 direct purchases of stock. And -- 17 Q. And when I looked at the -- when I 18 looked at it, I think that the purchases of 19 stock, you told me that you didn't see any 20 significant correlation. 21 A. Exactly. There was no impact on 22 the price for Rhino's purchase of stock. 23 Q. Okay. And there was no impact in 24 terms of the transactions when you looked at 25 those in isolation in your regression analyses.	1 - STEPHEN D. PROWSE - 2 principal purchases. 3 A. But potentially could have 4 affected the price. 5 Q. Okay. 6 A. But reasonable -- 7 Q. You don't know -- 8 A. That's what were tested. 9 Q. Okay. But you don't know? 10 A. I don't know what? 11 Q. I mean, isn't it a tautology? 12 That's what we're testing? I mean, the 13 question is, is the information public to have 14 an impact? Don't have you to, you know, come 15 to a conclusion of whether or not the 16 information could possibly have had an impact? 17 A. No, the question is, did Rhino's 18 presence in the marketplace have an impact on 19 the stock? Rhino was a large trader of this 20 stock. It had potentially a very large supply 21 of stock to sell into the market based on its 22 FP -- because it was an FPS holder. Market 23 participants would have understood that. 24 Rhino's presence is absolutely -- in the 25 marketplace is absolutely a potential factor in

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<p>1 - STEPHEN D. PROWSE - 2 determining the price because Rhino is an 3 important trader in Sedona stock. 4 Q. So, how can you conclude that it 5 didn't have an impact on the price of the stock 6 if what you just said was it was a major trader 7 and everybody perceived it as being a major 8 trader?</p> <p>9 A. Rhino was potentially a big trader 10 in Sedona stock. So that's why you want to 11 look at if, when it trades, it has an impact on 12 the stock. We find it doesn't.</p> <p>13 Q. Well --</p> <p>14 A. So that's what -- that's what the 15 data tell us. That's what we're testing.</p> <p>16 Q. Well, one of the data -- when you 17 talk about magnitude in impact, one of the 18 data's net daily trades. Right?</p> <p>19 A. One of the?</p> <p>20 Q. One of the regressions is net 21 daily trades?</p> <p>22 A. One of the regressions has net 23 daily trades in it.</p> <p>24 Q. Why isn't that significant in 25 light of what you just said about, you know,</p>	<p>1 - STEPHEN D. PROWSE - 2 entirely inappropriate. He's answering your 3 question. 4 MR. GUIDO: I think he keeps 5 avoiding the question. 6 BY MR. GUIDO: 7 Q. My question is, okay -- I have a 8 simple question for you. And it's just the 9 same question I had for Mr. Beloreshki, and I 10 believe he tried to avoid answering the 11 question. 12 And I want you to answer this 13 question: Is if you take net daily trades, 14 okay, and it shows a 95 percent significance of 15 the impact of Badian's trading, what is the 16 reason for rejecting that statistical analysis 17 which you've done here and you didn't even 18 include it because you say it was an oversight 19 in your report? 20 Explain to me why you exclude that 21 without all of this other discussion about 22 other things which you've testified are 23 statistically not significant to the impact of 24 Sedona stock. Just tell me with regard to that 25 one regression analysis why you rejected it and</p>
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<p>1 - STEPHEN D. PROWSE - 2 Amro's market power in the marketplace? 3 A. That's what the data tells you. 4 That's what you want -- that's what you use the 5 data to test. You have a theory. 6 Q. Okay. 7 A. And you want to test it. The 8 theory is Rhino's presence in the marketplace 9 potentially impacts the stock price. We want 10 to test that. We did test that. We found that 11 we could not -- we could not reject the null 12 hypothesis of no impact. 13 We did the same with Rhino's net 14 daily trades, and the same with Rhino's net 15 daily trades as a percentage of total volume. 16 Q. Did you -- 17 A. Again, we couldn't reject the 18 hypothesis. 19 Q. Well, did -- 20 A. Hang on. I'm not finished. 21 We couldn't reject the hypothesis 22 of no impact. 23 Q. I enjoy your filibustering, but I 24 do have a limitation of time -- 25 MR. SOHN: Mr. Guido, that's</p>	<p>1 - STEPHEN D. PROWSE - 2 why you didn't include it in -- in your report 3 and why you didn't explain why you excluded it 4 from your report. 5 MR. SOHN: Mr. Guido, the tone of 6 your question is entirely inappropriate. The 7 finger pointing is inappropriate. You're free 8 to ask whatever questions, you know that, but 9 there's an appropriate way to do it and an 10 inappropriate way to do it. 11 MR. GUIDO: I haven't said 12 anything inappropriate. 13 BY MR. GUIDO: 14 Q. Would you please answer the 15 question? 16 A. First of all, you claimed that I 17 didn't answer the question, and then you 18 changed the question. We can go back and ask 19 the court reporter what the question was that I 20 was answering when you went off on me. And you 21 will find that it's a different question than 22 you just asked me. 23 Q. Okay, let's -- 24 A. Secondly -- I'm not finished. 25 Secondly, you asked me about four different</p>

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1 - STEPHEN D. PROWSE - 2 questions. So please ask me a question one at 3 a time that I can answer. 4 MR. GUIDO: Will the court 5 reporter read back the question to the witness 6 who doesn't seem to understand. 7 MR. SOHN: Mr. Guido, I mean, the 8 comments are inappropriate. Your question goes 9 on for about four pages and -- and it's 10 entirely reasonable that the witness is going 11 to have a problem answering a four-page 12 question. 13 So if you could just ask a simple 14 question, a straightforward question, 15 Dr. Prowse is happy to answer it, as he's been 16 doing all day. 17 MR. GUIDO: All he has to say is 18 "I don't understand the question" -- 19 MR. SOHN: Which is what he just 20 said. 21 MR. GUIDO: He didn't say 22 that. 23 A. I did say that. I said you asked 24 me four questions and I don't know which one to 25 answer. So ask -- ask me one and I'll answer	1 - STEPHEN D. PROWSE - 2 significant? 3 A. Because after you adjust for the 4 fact that you're making multiple tests, you 5 have to adjust for the fact that multiple tests 6 complicate the interpretation of a "P" value. 7 This is a widely accepted scientific result. 8 Q. What's the literature support -- 9 MR. SOHN: Mr. Guido. 10 A. Now you interrupted me, so do you 11 want me to now answer the next question? 12 Q. Well, you just said you make an 13 adjustment for multiple tests. 14 A. You make an adjustment for 15 multiple tests. And when you make that 16 adjustment, it doesn't pass the Alpha 17 threshold. 18 Q. Okay. And what's the literature 19 that supports that? 20 A. There's a widely accepted 21 literature. It's in many standard statistical 22 text -- textbooks on multiple comparisons. 23 David Kaye and David Freedman have talked about 24 it in the Reference Guide on Statistics, which 25 is part of the Reference Manual of Scientific
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1 - STEPHEN D. PROWSE - 2 it. 3 Q. Fine. 4 MR. GUIDO: Can you read back the 5 question? 6 (Whereupon, the record is read 7 back.) 8 MR. SOHN: That's four questions. 9 MR. GUIDO: That's five. 10 A. I counted five. 11 Q. Okay. One -- 12 MR. SOHN: We agree it's more than 13 one. 14 MS. SCHECHTMAN: We accept your 15 apology, Mr. Guido. 16 MR. SOHN: Do you have a question? 17 BY MR. GUIDO: 18 Q. Why did you regret -- reject 19 Regression 5? 20 A. What do you mean by "reject"? We 21 didn't reject any regressions. 22 Q. Well, you deemed that it wasn't 23 significant, didn't you? 24 A. It was -- it's not significant. 25 Q. Okay. And why isn't it	1 - STEPHEN D. PROWSE - 2 Evidence that is issued by the Federal Judicial 3 Center, I believe; that multiple comparisons 4 complicate the interpretation of a "P" 5 statistic, of a probability statistic. And 6 that if you run 20 different regressions, you 7 shouldn't be surprised to find a spurious 8 correlation even when the null hypothesis is 9 true. 10 Q. What edition of David Kaye's piece 11 in the Reference Guide of Statistics are you 12 referring to? 13 A. I don't know. 14 Q. When did you read that? 15 A. I have a copy of it. I don't know 16 what edition it is. 17 Q. And you're -- you're saying that 18 David Kaye supports your view when there are 19 statistical -- that there are statistical 20 methods for coping with multiple looks at the 21 data. 22 Is that a fair assessment? 23 A. I don't remember reading that. I 24 remember reading that multiple comparisons 25 complicate the interpretation of a "P"

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1 - STEPHEN D. PROWSE - 2 statistic. And that if you do multiple tests, 3 you shouldn't be surprised to find a spurious 4 correlation when the null is true. 5 Q. Well, I have David Kaye in 2000, 6 and this is what David Kaye says in 2000. And 7 do you think this supports what you just said: 8 "There are statistical methods for coping with 9 multiple looks at the data which permit the 10 calculation of meaningful 'P' values in 11 certain cases." 12 Is that what you're referring to? 13 MR. SOHN: Mr. Guido, you're -- 14 first of all, I mean, you're asking the witness 15 about a document that you haven't shown him. 16 MR. GUIDO: Well, the -- 17 MR. SOHN: And you're -- and 18 you're pulling an excerpt out of it. So, I 19 mean, it's an unfair question. 20 MR. GUIDO: I'm making a 21 representation that that's a sentence that 22 appears in this -- in this piece. 23 BY MR. GUIDO: 24 Q. Is that what you're referring 25 to?	1 - STEPHEN D. PROWSE - 2 council. Okay? Take that example. 3 And, so, I decide that I'm going 4 to go out and do a survey of the residents of 5 lower Manhattan to get their view of whether or 6 not it should be rebuilt exactly the way it 7 existed before it came down. 8 And I go out and I do a survey. 9 You know, I apply all of the same appropriate 10 sampling methods and I come up with the answer 11 and I say, no, we don't want it rebuilt the way 12 it was. And I say, oh, boy. 13 So I commission another 14 statistical analysis, and they go out and they 15 come up with the same result. And, so, I end 16 up commissioning 20. So I come up with five of 17 the people that say, yes, I want it rebuilt. 18 Is what you're referring to -- and 19 I think your colleague referred to it as the 20 Bonferroni correction -- is that the situation 21 that is designed to apply to? 22 MR. SOHN: Objection to the form. 23 A. Well, I'm not sure I can reply to 24 your hypothetical. But the situation it's 25 supposed to apply to is when you have multiple
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1 - STEPHEN D. PROWSE - 2 A. I would have to see the context of 3 it. 4 Q. Why do you have to see the 5 context? Because you know -- 6 A. Because whenever -- because 7 whenever I'm quoted a sentence and asked what 8 it means, I like to see what the context is of 9 what's being talked about. 10 Q. Well, let me ask you this. I 11 mean, you -- you cited David Kaye. Anyone else 12 you want to cite? 13 A. There's a variety of articles out 14 there. Bonferroni, Dunn, Tukey. There's talk 15 about this in some -- in, I think, standard 16 statistical textbooks about multiple 17 comparisons. There's a variety of literature 18 out there on it. 19 Q. Well, let me ask you about the 20 literature. 21 Does the literature primarily 22 address this hypothetical, this situation? I 23 want to rebuild the World Trade Center just 24 exactly the way it was. So I -- and I want to 25 get support for that, to lobby the city	1 - STEPHEN D. PROWSE - 2 tests or multiple comparisons trying to find a 3 result and -- a universal result. 4 And the fact is that it's just -- 5 it's just the logic of statistics that if you 6 have -- the more regressions you run or the 7 more tests you do, the more likely you are to 8 find a spurious correlation. And you need to 9 control for that. 10 Q. The -- and what is the mathematics 11 that you do to control for that? 12 A. I think there are a variety of 13 different things you can do. There's the 14 Bonferroni correction; there's the Sidak 15 correction. They're very close, very similar. 16 There are -- 17 Q. Could you spell the second one? 18 A. S-i-d-a-k. 19 There are -- there are others that 20 are more subjective in terms of parsing the "P" 21 values across different tests, but the 22 Bonferroni correction is a very simple and 23 widely known correction to do. 24 Q. Have you read any of the 25 literature that's critical of the application

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1 - STEPHEN D. PROWSE - 2 of the Bonferroni correction? 3 A. I'm aware of some of it. 4 Q. And what does that literature say? 5 A. It generally says that, 6 particularly when you're doing extremely large 7 sampling, with very, very large number of 8 tests, that the Bonferroni correction can be 9 conservative. 10 Q. Have you ever read any literature 11 that indicates that the statistical methods for 12 coping with multiple looks of data would be of 13 little help in a case where analysts have run 14 through a variety of regression models to 15 arrive at the one considered the most 16 satisfactory? 17 MR. SOHN: You're asking if he's 18 ever read that sentence? 19 MR. GUIDO: No. 20 BY MR. GUIDO: 21 Q. Are you aware of literature that 22 indicates that that's a problem with using the 23 statistical approach? 24 A. I'm aware of literature -- the way 25 I interpret what you just said is what I've	1 - STEPHEN D. PROWSE - 2 drop a footnote in the report to that effect; 3 that this doesn't change my opinion because 4 this is a -- this is a spurious result as a 5 result of running a number of multiple tests 6 and because we need to control for that. 7 If you apply a Bonferroni 8 correction, it's -- this particular regression 9 still is not significant, as are -- as are none 10 of the -- as are all of the others not 11 significant. And, therefore, it doesn't -- 12 doesn't change my opinion. 13 I explained this morning that, 14 unfortunately, I forgot to drop that footnote 15 into the report before it issued. 16 Q. Well, isn't it -- isn't it 17 important for -- for an expert to include all 18 of the information that he bases his opinion on 19 in his report? 20 A. I don't often include all of the 21 analysis I do on a particular project in the 22 exhibits or in the text of my report. It 23 exists as a work sheet. It's a supporting work 24 sheet to either an exhibit or a piece of data 25 in the report.
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1 - STEPHEN D. PROWSE - 2 been saying for the past half an hour. And 3 that is that there's a -- there's a problem, 4 which is generally called data mining, which is 5 running multiple tests and then relying on one 6 in which you get a spurious correlation where 7 at -- where the result of the spurious 8 correlation is the fact -- simply the fact that 9 you've run multiple tests and the logic of 10 statistics tells you that you're getting hit a 11 spurious correlation for completely random 12 reasons even when the null is true. 13 Q. Well, did you actually do a 14 Bonferroni correction here? 15 A. I did. 16 Q. How come it's not in any of these 17 materials that were produced to me? 18 A. Well, the Bonferroni correction is 19 very easy to do. You -- all you do is adjust 20 the Alpha or the threshold "P" value by the 21 number of tests that you've run. 22 And when I -- when Erica reported 23 the "P" values to me, as I've discussed earlier 24 this morning, I noted that there was a "P" 25 value less than .05. And I reminded myself to	1 - STEPHEN D. PROWSE - 2 Q. So you don't think it's relevant 3 to the jury to know that you did a regression 4 analysis that showed there was a statistical 5 correlation between Badian's trading activities 6 and Sedona's stock price? 7 MR. SOHN: Asked and -- asked and 8 answered. You just asked the same question. 9 A. And what -- what I just said is I 10 do think it's important to know. And that's 11 why I wanted to put a footnote into the report, 12 but, unfortunately, I forgot. But I'm telling 13 you now. 14 Q. Well, don't you have quality 15 control at FTI? 16 A. We do have quality control. 17 Unfortunately, you know, no one's perfect and 18 this was my fault because I was the one in 19 charge of the -- the last hurdle of this report 20 in terms of issuing it. And it was my fault 21 that that did not get into the report. 22 Q. Well, did you ever make an 23 attempt to evaluate whether or not each of the 24 models that were the basis for each of the 25 regressions were less strong than any of the

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 other models?	2 there's no impact on Sedona's stock from any
3 MR. SOHN: Objection to the form.	3 measure of Rhino's trading.
4 A. I think they're all legitimate.	4 What we've got here is two
5 This is what Mr. Beloreshki and I discussed at	5 spurious results out of very, very many. Two
6 the beginning. We want to try to understand	6 results where the "P" value is greater than --
7 all the potential ways that Sedona's stock	7 less than .05, out of very, very many results,
8 price could be impacted by Rhino's trading and	8 both from the regression analysis and from the
9 Rhino's transactions. We want to understand	9 nonparametric and parametric analysis that tell
10 all the different ways that that could happen.	10 us that there is no effect, including your own
11 And we understood going in that	11 expert -- your own experts' specification of
12 that would mean we might get a spurious result.	12 our Regression 5, which shows the same thing
13 But, you know, that's -- that's the problem	13 which -- over a different period which shows no
14 with running multiple comparisons. Sometimes	14 statistically different effect.
15 you will get a spurious result when you -- when	15 Q. Well, maybe, you know, I don't
16 you run a lot of them.	16 understand your vernacular.
17 Q. Well, why --	17 What do you mean by a "parametric
18 A. But we wanted to cover all the	18 test"?
19 bases.	19 A. A parametric test is a test that
20 Q. I'm sorry. You did all of these	20 assumes a distribution of the underlying stock
21 regressions. Okay? And I think three of them	21 returns in this particular case. Basically we
22 include data that you don't even know whether	22 assume a normal distribution in a parametric
23 or not -- was in the marketplace, could	23 test.
24 potentially affect the market. You're just	24 Q. And what's the normal distribution
25 surmising that.	25 that you assumed here?
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 MR. SOHN: Objection to form.	2 A. It's normal. That it's normal.
3 MR. GUIDO: Let me finish.	3 Q. The distribution to what?
4 BY MR. GUIDO:	4 A. The distribution of stock returns
5 Q. And you also indicated, I think	5 over a period of time. The distribution, is it
6 you testified, that the magnitude of Badian's	6 a bell-shaped curve or not?
7 activity could be a relevant factor to	7 Q. And that that -- you knew
8 consider.	8 eventually we were going to get to my little
9 Why did you decide that the rules	9 graph.
10 of finding correlation were spurious and not	10 MR. GUIDO: I'd like to have this
11 the others?	11 marked as exhibit next number.
12 A. Because there's a -- there's a	12 (Whereupon, exhibit is received
13 potential to affect the stock price through any	13 and marked BP-26 for identification.)
14 mechanism of a Rhino trade.	14 BY MR. GUIDO:
15 Secondly, the results that we get	15 Q. I only hand you this because I
16 have to be adjusted for the fact that you're	16 wanted you to look at the little red graph
17 going to get a spurious correlation. We just	17 there.
18 didn't -- we just didn't run nine regressions	18 Is that what you were referring to
19 and rely on that. We wanted -- we wanted to	19 when you talk about normal distribution?
20 rely on all the statistical analysis we did,	20 A. A bell-shaped curve.
21 including the nine regressions.	21 Q. Okay. And is that an example of a
22 And when you do that and you make	22 bell-shaped curve, type curve?
23 a correction for the fact that you're testing	23 A. This is an example of a
24 this every which way, then you could -- then an	24 bell-shaped curve. The curve.
25 appropriate conclusion, I believe, is that	25 Q. Okay. And one of the things that

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1 - STEPHEN D. PROWSE - 2 you're doing with these statistical regressions 3 is to decide where the data falls on that 4 bell-shaped curve? 5 A. Well, now we're back to 6 regressions. I was talking about the 7 parametric analysis. 8 Q. Okay. 9 A. But -- 10 Q. Excuse me. 11 A. Okay. So if you want to go back 12 to the regressions, that's fine. 13 Q. No. Okay. How do you apply a 14 parametric analysis to that? 15 A. Well, a parametric analysis that 16 we do in our report basically tests the 17 difference between a particular distribution 18 between the effect of Rhino's trade -- the 19 affect of Rhino's buys versus sells on the 20 stock price and whether the stock price -- and 21 how much the stock price goes up or down based 22 on the buys versus the sells versus the -- 23 versus the days when Rhino doesn't trade. 24 Q. Okay. 25 A. This is in -- summarized in	1 - STEPHEN D. PROWSE - 2 What about buys at the offer as 3 opposed to no buys? 4 A. Buys at the offer versus no buys? 5 Q. Uh-huh. 6 A. I would have to think about that. 7 Q. Okay. Did you think about it when 8 you prepared that exhibit? 9 A. No, we thought this was the 10 appropriate way to do it. 11 Q. No, I understand that. But you 12 didn't think about the alternatives, did you? 13 A. No. 14 MR. SOHN: He just answered the 15 question. 16 A. I just said we felt this was the 17 appropriate way to conduct the parametric 18 test. 19 Q. And you just now said you'd have 20 to think about the alternative I gave you. 21 And my question is: Why didn't 22 you think about that when you did this 23 exhibit? 24 A. Well, I'd have to think about the 25 specific -- think about if that was a
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1 - STEPHEN D. PROWSE - 2 Exhibit -- in Exhibit 10, for example. 3 Q. Okay. Let me ask you a question: 4 Is there another way -- is there other ways -- 5 other data to analyze in that parametric test 6 that was done here? 7 MR. SOHN: Did other than what? 8 Q. Other than buys and sells and no 9 transactions. 10 A. There could be. This is the way 11 we did it. We felt this was the easiest way to 12 do it, to group the -- to group the 13 observations by buys and sells and nothing 14 happening. 15 Q. I just asked you whether there 16 were other ways. I didn't ask you why you 17 didn't do the other ways. 18 A. Okay. 19 Q. Let me ask my next question: What 20 are the other ways? What are the other data 21 points that you could include here? 22 A. I mean, there's all sorts of ways 23 you could group the data if you wanted to. 24 Q. Well, let me give you an -- let me 25 give you an example.	1 - STEPHEN D. PROWSE - 2 reasonable way. We thought this was the 3 reasonable way to do it. 4 Q. Okay. Fine. Tell me what the 5 other alternatives were that you thought 6 about. 7 A. I can't remember. There were -- I 8 mean, you could group by -- could group by the 9 extent to which the stock price moves versus a 10 buy and a sell. You could group, you know -- 11 you could create a finer distinction instead of 12 stock price moves between 0 and five, five and 13 ten, ten and 15. Something like that. 14 Q. Okay. 15 A. You could create as big a matrix 16 as you wanted in terms of buys and sells versus 17 some characteristic of a stock price. You just 18 have to be careful about the number of 19 observations or the expected value you would 20 get in each of those cells. 21 Q. Well, could you -- could you do 22 one of these -- what is it, Exhibit 10A? -- 23 using the percentage of volume, Sedona's 24 percentage of volume or Badian's percentage of 25 Sedona volume?

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 A. Rhino's percentage of Sedona	2 you have -- and it's supposed to be an analysis
3 volume. You might be able to do that.	3 of the proportion of Rhino volume to market
4 Q. Did you think about doing that?	4 volume, and then it has impacts on price
5 A. Well, we looked at that in our	5 returns. And that the -- a couple of questions
6 regression analysis, and we looked at that in	6 I have about -- about this study.
7 our Exhibit 13, I believe -- 14 -- 12. Exhibit	7 If you take a look at -- look
8 12. So that was covered in other exhibits.	8 between the 250 and the 300 percent range. You
9 Q. In Exhibit 12. Okay. Let's look	9 see that dot right above the black line?
10 at Exhibit 12.	10 A. Yeah.
11 And what did you conclude Exhibit	11 Q. What is that?
12 12 demonstrated?	12 A. That's a -- that's a data point.
13 A. That there was no significant	13 Q. So what you're saying is that
14 relationship between trading volume and Sedona	14 Rhino's trading volume was almost 300 percent
15 stock price returns.	15 of the total volume?
16 Q. Well, isn't this Exhibit 12 a	16 A. On that particular day.
17 graph of the Regression Number 5?	17 Q. It was? How'd -- how'd that
18 A. No, it's not.	18 happen?
19 Q. Well, it is a Regression Number 5	19 A. Volume is measured here as buys
20 for the larger time period, isn't it?	20 plus sells. So, on that particular day, buys
21 A. No, it's not.	21 plus sells would have -- may have -- would have
22 Q. It's not?	22 been greater than 300 percent. I think there's
23 A. No.	23 one day, actually -- I don't know if it's this
24 Q. This says this is a proportion of	24 day. I think there's one day in our database
25 Rhino volume to market volume.	25 where we observed Rhino volume being greater
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 A. Right.	2 than the market volume. And we're not sure of
3 Q. And isn't that -- Rhino's --	3 the reason why.
4 Sedona trades as a percentage of the total	4 Q. Well, I mean, how can that be?
5 volume?	5 A. Well --
6 A. No.	6 Q. I mean, my understanding --
7 Q. Well, did you do this for the	7 A. Well, if the statements -- if the
8 shorter period of time?	8 statements say a transaction occurred on this
9 A. Did we do Exhibit 12 for the	9 day, we have volume at a particular amount, we
10 shorter period of time? I don't believe we	10 can't reconcile that. So that is one data
11 did. We may have. If we did, it's in the work	11 point that may be -- may be problematic. But I
12 sheets.	12 don't know if it's this one.
13 Q. Pardon?	13 Q. Well, what is your understanding
14 A. If we did, it's in the work	14 of how the total volume reported on Bloomberg
15 sheets, but I don't believe we did.	15 is calculated?
16 Q. Well, I mean, just take Exhibit	16 A. For the NASDAQ, both sides of the
17 No. 12. I mean, this, to me, is a scattergram.	17 transaction are reported.
18 I don't know if that's an appropriate term.	18 Q. As one transaction.
19 But it looks I can a scattergram. You have all	19 A. So you may -- so you get some
20 these points --	20 double counting as you go through. You may
21 A. You could call it that.	21 get --
22 Q. Huh?	22 Q. What?
23 A. You could call it that.	23 A. You may get some double counting
24 Q. You have all of these points that	24 as you go through.
25 are all over this scattergram. Okay? And that	25 Q. Really?

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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	A. You may do.	2	time?
3	Q. You may?	3	A. We did nine --
4	A. Yeah.	4	MR. SOHN: Objection to the form.
5	Q. So the buys are reported to the	5	I think there are least three false
6	market?	6	assumptions in there and three or four
7	A. So volume may be -- may be double	7	questions in there.
8	what it's supposed to be.	8	A. That's correct, there are. But in
9	Q. Have you ever studied the audit	9	answer to your final question, we did nine in
10	trail reports on how the Bloomberg is developed	10	the long period and nine in the shorter
11	off of the audit trail reports?	11	period.
12	A. No, I have not.	12	Q. Okay. Fine.
13	Q. You have no idea how the Bloomberg	13	And is the reason you rejected the
14	data gets reported?	14	findings of statistical significance in the
15	A. I'd have to look and see.	15	three, in the shorter period of time -- one of
16	Q. But you can't tell us today?	16	which I think the literature we characterized
17	A. I can't tell you sitting here	17	as weak, that being the daily trading as a
18	today.	18	percentage of volume because it isn't at the 95
19	Q. Did you ever know?	19	percent significance level. The reason you
20	A. Yeah, I think I've known. I think	20	rejected those three is because you came up
21	I've known.	21	with 15 others that showed no statistical
22	Q. Did you ever -- did you ever do	22	significance?
23	any research on that question?	23	MR. SOHN: Objection;
24	A. I've read articles on that.	24	mischaracterizes the previous testimony.
25	Q. On the question?	25	A. Right, it does. We didn't reject
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1	- STEPHEN D. PROWSE -	1	- STEPHEN D. PROWSE -
2	A. Yeah.	2	any regression. We considered all the
3	Q. Have you ever read any of the	3	regressions. We set up the design of the study
4	NASDAQ guidance on riskless principal	4	to investigate the -- all the potential routes
5	transactions?	5	that Rhino's trades could impact Sedona's stock
6	A. No, I have not.	6	price.
7	Q. No?	7	After running all the regressions,
8	Well, you didn't do the	8	all 18 of them, we found that there was a "P"
9	scattergram for the shorter period of time?	9	value greater than .05 in two of them. Those
10	A. I'm saying I can't remember if we	10	are spurious correlations, and you can't use
11	did it. If we did it, it's in the work sheets.	11	them to deduce an impact on a stock price when
12	If it's not in the work sheets, we didn't do	12	you've got numerous other results that tell you
13	it.	13	that there's no impact.
14	Q. Now, I'm still a little puzzled by	14	Q. Well, why are those spurious? And
15	what it is that you did that led you to	15	why -- why not the others be spurious?
16	conclude that the three analyses that showed	16	A. The others aren't spurious -- the
17	correlation -- or significant -- excuse me. I	17	others -- the others failed to reject the --
18	you used the "C" word and I'm sorry, Mr. Sohn	18	failed to -- failed to reject the null on their
19	and Mr. Glosten.	19	face. They have "P" values that are sometimes
20	That you rejected the three in the	20	very high.
21	shorter period of time. And your reason for	21	It's a generally accepted
22	doing that is because, in the longer period of	22	principle that when you run multiple tests and
23	time, you didn't show any statistical	23	you get -- you should expect to get -- just by
24	significance for -- was it nine regressions you	24	the nature of statistics, you should expect to
25	said that you did for the longer period of	25	get a spurious correlation now and again. And

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 if you properly adjust for that, you get --	2 Q. -- that you said that they
3 what you get from the entire battery of tests	3 prepared. And that it reject -- it failed to
4 is the fact that there's the conclusion that	4 reject the null hypothesis?
5 there's no impact.	5 A. That's my understanding, yeah.
6 Q. So --	6 But --
7 A. And, again, I would say that's	7 Q. What were the -- and it was net
8 confirmed by your own experts who ran the	8 daily trades?
9 Number 5 regression on a shorter period of time	9 A. I believe -- that's my
10 than we did and found -- and found on its face	10 understanding. I believe so.
11 a "P" value greater than .05, greater than 5	11 Q. Now -- so, based on that result
12 percent. That just shows you how spurious this	12 and the fact that you came up with 15 other
13 correlation is.	13 results, you rejected the three analyses that
14 Q. So you're saying that Professors	14 found a statistically significant relationship
15 Glosten and Jones ran the regression of the net	15 between Badian's trading activity and Sedona's
16 daily trades for a shorter period of time and	16 stock price?
17 found that their hypothesis couldn't -- that	17 MR. SOHN: Objection;
18 their analysis could not be checked? The null	18 mischaracterizes the testimony again.
19 hypothesis.	19 A. Yeah, you have mischaracterized my
20 A. Correct. It's in their work	20 testimony. We did not, for the third or fourth
21 sheets.	21 time, we did not reject any regressions. We
22 Q. It's in their work sheets? Which	22 considered all the regressions as a family
23 work sheet?	23 based on the fact -- and based on the fact that
24 A. Well, I don't know.	24 the "P" values for most of our regressions --
25 Q. Well, I mean, you're the one who's	25 and, by the way, all our nonregression
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 making the allegation and I just want to know	2 statistical analysis -- is greater than .05.
3 what you're talking about.	3 The "P" values that are greater
4 A. Well, I told you what I know. And	4 than .05 are clearly spurious correlations.
5 I can't identify the particular page, but --	5 And when you do multiple comparisons, you need
6 Q. Is it in --	6 to adjust for that danger. When you run --
7 A. -- if I'm right, I'm right; and if	7 when you run an extra regression, you increase
8 I'm wrong, I'm wrong.	8 the chance of finding a statistically -- or a
9 Q. Is it in their report?	9 "P" value of greater than .05.
10 A. No.	10 Q. And --
11 Q. Oh, it's not in their report?	11 A. Less -- less than .05.
12 A. No.	12 Q. And doesn't the literature suggest
13 Q. Where is it?	13 that to determine which of those are the
14 A. It's in the work sheets that they	14 regressions that should be relied upon for your
15 produced.	15 conclusions that you look to how the model has
16 Q. And it's -- it's in the work	16 been developed?
17 sheets that they produced to whom?	17 A. Well, presumably the models that
18 A. To us.	18 you are developing hypothetically -- in your
19 Q. And in those work sheets, you said	19 hypothetical are all appropriate models for
20 it was a shorter period of time?	20 looking at the impact or whatever relationships
21 A. I believe it was through -- I	21 you're trying to find.
22 think it was the month of March.	22 Q. Well, aren't some models more
23 Q. So it was March 1st through March	23 powerful than others?
24 30th was the regression --	24 A. Some may be.
25 A. Maybe, yeah.	25 Q. Well, what does the concept of

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 power mean when you're talking about comparing</p> <p>3 different regressions? Not the results of the</p> <p>4 regressions, but power when you're trying to</p> <p>5 decide whether the Regression 1, 2, 3, 4, 5, 6</p> <p>6 are more or less powerful than any of the</p> <p>7 others?</p> <p>8 A. Well, that doesn't have to do with</p> <p>9 the economic theory behind the variables. It</p> <p>10 has to do with the ability of the regression to</p> <p>11 find a relationship or not.</p> <p>12 MR. SOHN: May I make a</p> <p>13 suggestion? Just because I know they lock the</p> <p>14 door at six and it's ten to six right now. So</p> <p>15 maybe now's a good time for five minutes.</p> <p>16 MR. GUIDO: We'll take a break.</p> <p>17 THE VIDEOGRAPHER: This concludes</p> <p>18 Tape Number 4 in the videotaped deposition of</p> <p>19 Dr. Stephen Prowse. Going off the record at</p> <p>20 5:52 p.m.</p> <p>21 (A recess is taken.)</p> <p>22 THE VIDEOGRAPHER: This begins</p> <p>23 Tape Number 5 in the videotaped deposition of</p> <p>24 Dr. Stephen Prowse. Going back on the record</p> <p>25 at 6:05 p.m.</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 towards finding -- towards -- I don't believe</p> <p>3 he had any biases, as neither do I. We</p> <p>4 discussed the appropriate regression models to</p> <p>5 run in this matter. We agreed on them and we</p> <p>6 ran them.</p> <p>7 Q. Well, did you read The Frontiers</p> <p>8 of Convertible Financing that he wrote with</p> <p>9 Caryn Schechtman?</p> <p>10 A. Yes.</p> <p>11 Q. Did that indicate to you that he</p> <p>12 had any biases?</p> <p>13 A. No, that didn't indicate to me he</p> <p>14 had any bias. I regard him as a very, very</p> <p>15 accomplished economist and statistician who has</p> <p>16 a former trading background. And I value his</p> <p>17 opinion very highly and I think he's a very --</p> <p>18 he has a very high level of integrity in terms</p> <p>19 of running empirical analyses.</p> <p>20 Q. Okay. Is the existence of a bias</p> <p>21 by an expert something that the jury should be</p> <p>22 concerned about?</p> <p>23 MR. SOHN: Objection.</p> <p>24 A. Well, I don't know what you mean</p> <p>25 by bias. I know I'm not biased. I know</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 BY MR. GUIDO:</p> <p>3 Q. Now, Mr. Prowse, when -- when you</p> <p>4 first came into working on the Sedona matter,</p> <p>5 in all of the -- had the 18 regression analyses</p> <p>6 been done?</p> <p>7 A. I don't know what had been done</p> <p>8 prior to me getting involved. I know some of</p> <p>9 the -- some or all of the nine specifications</p> <p>10 or the nine regression models that</p> <p>11 Mr. Beloreshki and I decided were appropriate</p> <p>12 to run in this matter had been run previously,</p> <p>13 but I don't know over what time periods those</p> <p>14 regressions --</p> <p>15 Q. Do you know --</p> <p>16 A. -- had been run.</p> <p>17 Q. -- who selected those?</p> <p>18 A. I believe it was Mr. Beloreshki.</p> <p>19 Q. Okay. Did you ever attempt to</p> <p>20 determine whether or not he had any biases?</p> <p>21 A. I don't know what you mean by</p> <p>22 whether he had any biases.</p> <p>23 Q. A bias towards -- towards finding</p> <p>24 a null hypothesis.</p> <p>25 A. I don't believe he had a bias</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Mr. Beloreshki isn't biased in any manner.</p> <p>3 We're economists. We perform economic and</p> <p>4 financial analysis, and we are guided by</p> <p>5 what that economic and financial analysis</p> <p>6 tells us.</p> <p>7 Q. Okay. What percentage of your</p> <p>8 income in the last five years has come from</p> <p>9 activities other than fees for testifying as an</p> <p>10 expert witness?</p> <p>11 MR. SOHN: Objection to the form.</p> <p>12 A. That's a question I can't answer</p> <p>13 because I don't get paid on the basis of fees</p> <p>14 that I generate for expert witness work versus</p> <p>15 other work that I do. I get paid a salary by</p> <p>16 FTI for performing a variety of different</p> <p>17 economic and financial analyses, some of which</p> <p>18 are involved in litigation or disputes; some of</p> <p>19 which is not.</p> <p>20 Q. Okay. Well, what percentage is</p> <p>21 involved in litigation or disputes of the work</p> <p>22 that you've done over the last five years?</p> <p>23 A. Over the last five years, I would</p> <p>24 say -- I don't know what time period you're</p> <p>25 talking about within those five years, but on</p>

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2 average I would say maybe about 50 percent is	2 Q. Well, there was a disk that was
3 litigation or dispute related. There may or	3 provided to the SEC last night.
4 may not be a litigation. There may be a	4 Do you know that?
5 potential dispute between two parties, and I'm	5 A. Yes, I believe I do know it.
6 hired before litigation to maybe find an answer	6 Q. Okay. And you participated in
7 that might be acceptable to both parties, but	7 preparing that disk. Correct?
8 there's the potential for a lawsuit there.	8 A. I instructed that certain files be
9 Q. What about in the last two	9 put on that disk, right.
10 years?	10 Q. How many files were put on that
11 A. I would say probably the same. I	11 disk?
12 don't really -- I don't really track how much	12 A. I don't know the total because I
13 of my time is on one type of project versus	13 was only a part of the production. But I know
14 another type of project.	14 that my production -- I understand that my
15 Q. How important is the timeliness	15 production was from the Pet Quarters file,
16 of the disclosure of the material that you	16 basically, that you requested and that we
17 relied upon to the credibility of an expert	17 produced.
18 witness?	18 And I'll tell you right now that
19 A. I don't understand the question.	19 99 percent of what I produced is completely
20 Q. Well, you testified in how many	20 irrelevant to what -- to the issues in this
21 matters?	21 matter, because it has to do with our response
22 A. At trial?	22 to a Pet Quarters expert who basically did a
23 Q. Uh-huh.	23 valuation analysis or a damages analysis. But
24 A. I don't know. A dozen, maybe a	24 we decided to give it to you because we didn't
25 little more than a dozen.	25 want to -- even though it was completely
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 Q. And have you ever had a situation	2 irrelevant, we didn't want to -- we just wanted
3 where you produced documents the night before	3 to give it to you.
4 your deposition?	4 Q. Did the magistrate think it was
5 A. Yes.	5 irrelevant?
6 Q. You have?	6 A. Did the who?
7 A. Uh-huh.	7 Q. The magistrate.
8 Q. Did the opposing party object to	8 A. Well, I don't know what the
9 that?	9 magistrate decided, but we were asked to
10 A. I can't remember them objecting,	10 produce our Pet Quarters file. And even though
11 no.	11 I knew it was going to be completely
12 Q. How often has that happened?	12 irrelevant, I said fine. So I can guarantee
13 A. More than once.	13 you that 99 percent of what I produced on there
14 Q. How voluminous was the material	14 you needn't waste any time on because it
15 that was produced the night before?	15 doesn't address --
16 A. I can't tell you.	16 Q. Do you know how many files were
17 Q. Do you know how voluminous the	17 included?
18 material was that was produced to the SEC last	18 A. From what --
19 night at 8:07?	19 MR. SOHN: Asked and answered.
20 A. Are you referring to the GOJO	20 A. From what I produced?
21 documents or the RA documents or something	21 Q. Yeah.
22 else?	22 A. I can't tell you the number of
23 Q. The disk.	23 files. I know we did a lot of work on Pet
24 A. What do you mean by "the disk"? I	24 Quarters on the valuation or damages piece, so
25 don't know what you mean by "the disk."	25 I expect there were a lot of files. But I can

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2 tell you now you can save time by not going	2 those files which you say are totally
3 through them because you won't find them of	3 irrelevant, on a disk with over eight hundred
4 interest. At least I don't believe you'll find	4 files, would that have made it difficult for me
5 them of interest unless you're interested in	5 to find the files to question you today?
6 valuation and damages analyses.	6 MR. SOHN: Objection to the
7 Q. Do you know -- do you know how	7 suggestion in the question.
8 large in terms of gigabytes the files were that	8 A. I can't -- I can't speak to that
9 were produced last night?	9 question. I don't know exactly how many files
10 A. I can't tell you how large they	10 were part -- were my production with regards to
11 are. I can just tell you what I produced in	11 the valuation/damages analysis of Pet Quarters.
12 terms of substance, content.	12 I'm not -- I don't know how quick you are with
13 Q. Do you have a -- is there a limit	13 your computer.
14 on your -- do you have an Outlook file?	14 Q. Well, no matter how proficient I
15 A. Do I have an -- you mean an	15 am with a computer, do you think that anyone
16 e-mail?	16 could have gone through two gigabytes of
17 Q. An e-mail Outlook file.	17 documents to prepare for your deposition today
18 A. Yeah.	18 if they received them at eight o'clock last
19 Q. And you allow -- are you allocated	19 night?
20 a certain size on the server for that Outlook	20 MR. SOHN: Objection.
21 file?	21 A. I'm -- I can't answer that
22 A. For my e-mail file?	22 question. Sorry.
23 Q. Uh-huh.	23 Q. Well, you've worked with data,
24 A. I presume -- I presume so. I	24 haven't you?
25 don't know.	25 A. Yeah.
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 Q. Do people at FTI have certain	2 Q. I mean, you have a sense of how
3 space, size limitations, on what they can put	3 quickly you can go through files, don't you?
4 on the servers at FTI?	4 A. Yeah. And if you -- I don't know
5 A. I just don't know the answer to	5 how the files were organized and I don't know
6 that.	6 what the titles of them were on. But if you
7 Q. Would it surprise you that the	7 had read the Pet Quarters report closely, which
8 disk that was produced to us last night had	8 was produced weeks ago, you would know that we
9 over eight hundred files on it?	9 had a substantial amount of analysis that was
10 A. I can't speak to what was put on	10 devoted to rebutting a plaintiff's expert
11 there apart from what I put on there. I know	11 called Mr. Trugman, who did a valuation and
12 we did a lot of work on the valuation and	12 damages analysis.
13 damages aspect of the Pet Quarters matter. And	13 And to the extent that you can
14 you're free to look at it, but I can tell you	14 identify quickly files on that disk that relate
15 now you probably don't want to waste too much	15 to Trugman and valuation and damages, I would
16 time on it.	16 think, clearly, that you wouldn't want to spend
17 Q. Well, would the existence of all	17 any time with them.
18 of those files on that disk last night have	18 Q. Well, taking the files that you
19 made it impossible for me to go through the	19 produced, how were they described?
20 files to find files that are relevant to ask	20 A. I can't tell you. I don't know
21 you questions today?	21 how they were organized. There was probably
22 A. Was that a question?	22 some logic to them and there was probably
23 Q. Yeah.	23 some -- there was probably some names that --
24 A. What is the question?	24 that I would recognize in terms of the types of
25 Q. Well, is the existence of all of	25 analysis that went into the Trugman analysis

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 and that you may have read if you were familiar</p> <p>3 with the analysis we did in Pet Quarters with</p> <p>4 regards to the valuation analysis.</p> <p>5 Q. I looked at this disk and I spent</p> <p>6 a fair amount of time looking at this disk, and</p> <p>7 there are no files in here that have a</p> <p>8 description on the file, when I open up the</p> <p>9 disk, that say that this is the damages</p> <p>10 analysis from Pet Quarters.</p> <p>11 Did you -- when you provided the</p> <p>12 disk, did you provide a description with them</p> <p>13 so that they could be easily reviewed to</p> <p>14 determine which ones were relevant for your</p> <p>15 testimony today?</p> <p>16 MR. SOHN: Objection.</p> <p>17 A. I just asked for the files to be</p> <p>18 produced. I would assume they would just be</p> <p>19 produced as they existed on our server.</p> <p>20 Q. And didn't the files exist on your</p> <p>21 server under the numbering system "BP" and then</p> <p>22 a number?</p> <p>23 A. No, they didn't exist under a "BP"</p> <p>24 number. They existed in the Pet Quarters files</p> <p>25 under probably various different subfolders</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 just don't know. I can't tell just by the name</p> <p>3 of the author.</p> <p>4 Q. Have you read any articles on the</p> <p>5 impact of various trading strategies on stock</p> <p>6 prices?</p> <p>7 A. I don't know exactly what you mean</p> <p>8 by that.</p> <p>9 Q. Well, I mean, when you -- when you</p> <p>10 prepared your report, you cite one article that</p> <p>11 you reviewed in your -- in Exhibit No. 2. I</p> <p>12 remember last night, as I was stumbling through</p> <p>13 the two-gigabyte file and I was not able to</p> <p>14 retract it, that I found another example --</p> <p>15 another sheet of material that you had</p> <p>16 considered, or somebody had purportedly</p> <p>17 considered, when they prepared the expert</p> <p>18 report. And it included a great number of</p> <p>19 other articles.</p> <p>20 Was there -- was there a lot of</p> <p>21 literature that you read to prepare your expert</p> <p>22 report that are not listed in what you</p> <p>23 considered there?</p> <p>24 MR. SOHN: In this case?</p> <p>25 MR. GUIDO: In this case.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 with different pieces of analysis in them.</p> <p>3 Q. Well, did the subfolders mention</p> <p>4 the subject matter of each of the files?</p> <p>5 A. I would have to go back and look</p> <p>6 at the folder to tell you that.</p> <p>7 Q. So you don't know. All right.</p> <p>8 A. I don't know sitting here.</p> <p>9 Q. The -- with regard to the issue of</p> <p>10 multiple statistical regressions, have you ever</p> <p>11 read any articles where he explains what was</p> <p>12 wrong with the Bonferroni adjustment?</p> <p>13 A. I've read articles that discuss</p> <p>14 the Bonferroni adjustment.</p> <p>15 Q. Have you ever read any article by</p> <p>16 Thomas Perneger, P-e-r-n-e-g-e-r?</p> <p>17 A. If you show me the article, I</p> <p>18 could look at it. I may have.</p> <p>19 Q. But you don't recall reading it?</p> <p>20 A. I don't recall that specific name,</p> <p>21 but I may well have read the article.</p> <p>22 Q. Have you ever -- are you aware of</p> <p>23 an article by Kenneth Rothman on no adjustments</p> <p>24 are needed for multiple comparisons?</p> <p>25 A. I may have read that article. I</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 A. I can't recall seeing -- I can't</p> <p>3 recall creating an Exhibit 3, which would be</p> <p>4 the exhibit that details the documents</p> <p>5 reviewed, that lists a large number of</p> <p>6 articles. I just can't remember them being</p> <p>7 there.</p> <p>8 I do know that the Chaplinsky</p> <p>9 article was one I definitely reviewed in the</p> <p>10 context of performing this report.</p> <p>11 I am also just generally aware of</p> <p>12 other articles that I didn't refer to</p> <p>13 specifically for this report, but I -- that</p> <p>14 formed the background of my professional</p> <p>15 knowledge of FPS securities.</p> <p>16 Q. Well, let me ask you a question:</p> <p>17 Is there any literature or paper that you've</p> <p>18 read that supports the running of Regression</p> <p>19 Number 1 that you did in this case?</p> <p>20 A. A specific article or report?</p> <p>21 Q. Yeah.</p> <p>22 A. Not sitting here that I can think</p> <p>23 of one.</p> <p>24 Q. Is there any that supports the</p> <p>25 running of Regression Number 2?</p>

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 A. Let me look at what Regression	2 offer?
3 Number 2 is.	3 A. I believe that's correct.
4 Well, generally there are articles	4 Q. Okay. And -- but you didn't do
5 that look at flags for whether someone is in	5 that when you did your regression, did you?
6 the market or whether someone buys or sells.	6 A. No. We -- we looked at Rhino's --
7 There are many articles that have flags for	7 whether Rhino just bought. We wanted to be as
8 that, when looking at the impact of a trade.	8 comprehensive as possible.
9 Q. Can you give us an example?	9 Q. You didn't look to determine
10 A. Well, articles written by	10 whether or not it was at the bid or the offer
11 Professors Glosten and Jones have, in some of	11 or where it was in that range?
12 their regressions specifications, have flags	12 A. We did not do that.
13 for whether someone buys or whether someone	13 Q. Okay. Now, with regard to
14 sells -- or what they determine to be a	14 Regression Number 3, is there any literature
15 seller-initiated trade or a buyer-initiated	15 that supports the running of Regression Number
16 trade.	16 3?
17 And in much of the market	17 A. Well, all Regression 3 is, is --
18 microstructure literature, there are	18 Regression 3 differs from Regression 2 by also
19 specifications that have flags or dummies for	19 looking at transfers in principal and direct
20 that type of -- for measuring that activity.	20 purchases of stock. And there's certainly a
21 Q. Well, in the literature that you	21 lot of literature out there that tells you that
22 saw simply flags for buys or sells, or buys	22 when an entity issues stock, that is an
23 that are identified as buys because they're at	23 important piece of information for the market.
24 the offer and sells because they're at the bid?	24 Q. Well, that's public issuances.
25 A. They're -- they're certainly --	25 Right? That literature --
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 they're certainly dummy variables. They don't	2 A. It's public issuances of stock.
3 have anything to do with volume. But, as I	3 But, again, if the market knows about it,
4 said in my last answer, based on a particular	4 because Rhino is a big player in this market,
5 definition of what a buy is will determine	5 then that would, in turn, be an important piece
6 whether that zero-one dummy is a buy or is a	6 of information for the market.
7 zero or a one.	7 Q. Okay. But you don't have any
8 Now, there may be different	8 information that the Rhino or Amro purchases
9 definitions of how you define a buy that --	9 were -- was information that was available to
10 that differ across the literature. I'm not	10 the public?
11 certain whether there are or not.	11 A. We did not do that determination,
12 Q. Well, I mean in terms of the	12 but that's -- that's part of the reason we're
13 literature definitions of buy, do you know of	13 testing it, because we wanted to cover all our
14 any literature that uses your definition of	14 bases here.
15 buy? Just a simple buy as opposed to a	15 Q. Well, but if it turns -- one of
16 transaction at the bid?	16 the reasons that you could determine not to
17 A. There may be. I can't think of --	17 have a significance is that that information
18 Q. But you --	18 could have turned out not to have been
19 A. I can't think of a piece of	19 available to the market. Isn't that true?
20 literature as I sit here.	20 A. Actually, that's wrong, because
21 Q. But Mr. Glosten, Professor	21 the more regressions you run, the in -- the
22 Glosten, has written papers on the use of	22 more likely you are to get a spurious result.
23 analyzing trades by characterizing them as	23 So you run an additional regression, the more
24 buys. And in those papers didn't he define	24 likely you are to get a spurious result.
25 buys as transactions at the bid -- at the	25 Q. Well, is there an incentive to run

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 spurious regressions so that you could get a</p> <p>3 spurious result?</p> <p>4 A. A spurious result would be a</p> <p>5 result that has a "P" value of less than .05,</p> <p>6 which would, if interpreted incorrectly, would</p> <p>7 be viewed as price impact. And that is what</p> <p>8 we're trying to avoid here. We're trying to</p> <p>9 avoid data mining.</p> <p>10 Q. And one of the -- and one of the</p> <p>11 ways to do data mining is to run regressions</p> <p>12 that you know are going to result in no</p> <p>13 significant relationship, isn't it?</p> <p>14 A. No, I would say data mining is the</p> <p>15 opposite of that. I would say data mining is</p> <p>16 running regressions until you find a</p> <p>17 significant relationship and then that's</p> <p>18 your -- that's your model.</p> <p>19 Q. What was the first regression that</p> <p>20 was ever run of Sedona's stock price in</p> <p>21 relationship to Badian's activity?</p> <p>22 A. Well, I can't speak to that</p> <p>23 because if you're talking about -- well, are</p> <p>24 you talking about at FTI or are you talking</p> <p>25 about prior to FTI?</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 report?</p> <p>3 A. I didn't search for any articles</p> <p>4 on the PIPEs market for this specific</p> <p>5 engagement. I was aware of, just based on my</p> <p>6 professional knowledge in the economics and</p> <p>7 finance literature, I've been aware of a number</p> <p>8 of articles out there that are -- that speak to</p> <p>9 future price securities. And I've talked about</p> <p>10 at least one of them earlier this morning.</p> <p>11 Q. I think one of them was an article</p> <p>12 by Hillion?</p> <p>13 A. Hillion and Vermaelen.</p> <p>14 MR. GUIDO: I'd like to have</p> <p>15 marked as the exhibit next number an article by</p> <p>16 Hillion and Vermaelen.</p> <p>17 (Whereupon, exhibit is received</p> <p>18 and marked BP-27 for identification.)</p> <p>19 BY MR. GUIDO:</p> <p>20 Q. Is this the article that you were</p> <p>21 referring to?</p> <p>22 A. Yes.</p> <p>23 Q. Does the paper exclude the</p> <p>24 possibility that someone would or could</p> <p>25 manipulate the stock price to take advantage of</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. Ever.</p> <p>3 A. Well, I don't know.</p> <p>4 Q. You don't know.</p> <p>5 So Regression Number 5, the one</p> <p>6 that found the significant relationship, could</p> <p>7 have been the first regression that was run.</p> <p>8 Right?</p> <p>9 A. It certainly wasn't the first</p> <p>10 regression run. When we did our analysis at</p> <p>11 FTI, we ran all of the regressions.</p> <p>12 Q. Simultaneously or --</p> <p>13 A. We instructed for them all to be</p> <p>14 run.</p> <p>15 Q. Right. Okay. But that's after</p> <p>16 they had already been run once before.</p> <p>17 Right?</p> <p>18 A. That's -- that's after they had</p> <p>19 been run once before, but I'm not sure on the</p> <p>20 same time periods that we ran them on -- at</p> <p>21 FTI.</p> <p>22 Q. When -- did you search for any</p> <p>23 literature on the PIPEs market for financial</p> <p>24 future price securities other than the one</p> <p>25 article that you cite in your -- in your expert</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 a low conversion price?</p> <p>3 MR. SOHN: Does it say that that's</p> <p>4 not possible? Is that the question?</p> <p>5 MR. GUIDO: Yeah.</p> <p>6 A. Well, this is a 35-page article</p> <p>7 with -- and although I'm very aware of it, I</p> <p>8 don't know every single piece of analysis or</p> <p>9 conclusion they come to. So, I can't speak to</p> <p>10 that.</p> <p>11 I know, basically, the focus of</p> <p>12 the -- of the paper, the thrust of the paper,</p> <p>13 in my opinion, is to demonstrate the fact that</p> <p>14 floating price convertibles are issued by very</p> <p>15 risky firms and are, therefore, very risky for</p> <p>16 investors that hold them.</p> <p>17 Q. And isn't it -- does it also talk</p> <p>18 about the firm -- that they are firms that</p> <p>19 stock prices are very responsive to external</p> <p>20 events?</p> <p>21 A. It -- it may talk about that.</p> <p>22 You'd have to point me to exactly where that</p> <p>23 is. I can't recall that. But certainly the</p> <p>24 stock prices of these companies, just like</p> <p>25 Sedona's, are very volatile.</p>

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 Q. Have you ever studied any	2 financial innovations aimed at resolving
3 literature on -- on the -- what's referred to	3 asymmetrical information problems in small,
4 as the scalping phenomenon in trading?	4 risky firms. In theory, a floating price
5 A. The scalping phenomenon?	5 convertible is ideal for such firms. In
6 Q. Uh-huh.	6 practice, the stocks of such firms are illiquid
7 A. I may have in the past. I can't	7 and subject to manipulation by short sellers
8 remember sitting here.	8 and hedge funds. The floating price
9 Q. Well, have you ever heard the term	9 convertible may, thus, produce a downwards
10 "pump and dump"?	10 spiral in the stock price."
11 A. Yes.	11 Do you see that?
12 Q. In what context?	12 A. Yes.
13 A. In the context of the SEC bringing	13 Q. Do you agree with it?
14 litigation against individuals for alleging	14 A. Yeah, I think the stocks of such
15 pump-and-dump schemes.	15 firms could be subject to manipulation. I
16 Q. Have you ever seen any statistical	16 don't rule that out.
17 analyses or regression analyses of the impact	17 Q. Oh, okay. The -- on the
18 of those pump-and-dump schemes?	18 Bonferroni adjustments, I'd like to hand you
19 A. I haven't seen any statistical --	19 the Perneger article.
20 do you mean statistical analyses on the	20 MR. GUIDO: And may I have it
21 frequency of them or -- the frequency of the	21 marked as Exhibit No. 28?
22 suits or statistical analysis in a particular	22 (Whereupon, exhibit is received
23 pump-and-dump --	23 and marked BP-28 for identification.)
24 Q. Of the impact --	24 MR. SOHN: Do you have another
25 A. -- scheme?	25 copy?
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 Q. Of the impact of them.	2 MR. GUIDO: Oh, excuse me.
3 A. I don't believe I have. I may	3 MR. SOHN: Thank you.
4 have, but I can't remember.	4 BY MR. GUIDO:
5 Q. Do you consider the production of	5 Q. Have you ever read this Perneger
6 this disk that I received at eight o'clock to	6 article? Perneger.
7 be a timely disclosure under the court order in	7 A. I may have. It looks somewhat
8 the subpoena issued against you in this case?	8 familiar, but I can't say for certain.
9 MR. SOHN: Objection.	9 Q. Well, I think you testified
10 A. I don't know what the time -- what	10 earlier that one of the things that you did was
11 would be considered a timely disclosure or not.	11 apply the Bonferroni adjustment to determine
12 It's a -- it's a disclosure. If there was a	12 that the Regression 5 was, I think, spurious, I
13 gap in what was produced before, I apologize.	13 think was your term?
14 And we've produced to you a supplement. And,	14 A. Spurious correlation.
15 like I said, most, if not all, of what I	15 Q. Yeah.
16 produced to you I would consider to be not	16 Can there be a spurious
17 relevant to this case, but you're free to look	17 noncorrelation?
18 at it.	18 A. Well, generally I think that's not
19 Q. Take a look at the Hillion	19 the problem. I think the problem is spurious
20 article, which is Exhibit 27, at page 384. Do	20 correlations.
21 you see the paragraph that says, "This paper	21 Q. I understand --
22 makes several contributions..."?	22 A. So I'm not -- I'm not sure whether
23 A. Yes.	23 there could be or could not be in a
24 Q. And the first one, it says, "It	24 hypothetical. But certainly there's not a
25 illustrates the difficulties of designing	25 spurious noncorrelation here since the vast

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<p>1 - STEPHEN D. PROWSE -</p> <p>2 majority of all our results show no impact and</p> <p>3 the vast minority do. And, so, that would</p> <p>4 be -- that would be -- those would be the</p> <p>5 spurious correlations.</p> <p>6 Q. Well, is a -- is a spurious</p> <p>7 correlation one in which you have a variable</p> <p>8 that you don't know what -- whether it actually</p> <p>9 had an impact in the market, or could likely</p> <p>10 have an impact on the market?</p> <p>11 A. No, that's not a spurious</p> <p>12 correlation. Not the way you asked that</p> <p>13 question.</p> <p>14 Q. What if Andreas Badian had -- had</p> <p>15 lent Sedona \$35 million in cash and it wasn't</p> <p>16 public? And you included that in your</p> <p>17 regression analysis on the stock price of</p> <p>18 Sedona. Would that be a spurious</p> <p>19 regression?</p> <p>20 MR. SOHN: Objection. The</p> <p>21 question is whether he lent a public company</p> <p>22 money and it wasn't publicly known that he lent</p> <p>23 the public company money?</p> <p>24 MR. GUIDO: That's correct.</p> <p>25 A. I can't answer the question the</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 legitimate.</p> <p>3 Q. So, you're saying the Bonferroni</p> <p>4 method is less legitimate when there are large</p> <p>5 number of tests that are being looked at?</p> <p>6 A. May be more problematic when you</p> <p>7 have thousands of tests or large numbers of</p> <p>8 tests.</p> <p>9 Q. And not when you have a smaller</p> <p>10 number of tests?</p> <p>11 A. Right. That's just the way the --</p> <p>12 the statistics work. And that's -- that's</p> <p>13 verified in the literature. I mean, that's</p> <p>14 talked about in the literature, Bonferroni.</p> <p>15 Q. Really? What literature?</p> <p>16 A. I can't cite an article right off</p> <p>17 the top of my head, but I do understand that's</p> <p>18 part of the issue, or that's part of the</p> <p>19 literature.</p> <p>20 Q. Well, I mean, this article,</p> <p>21 okay -- take a look at the paragraph that says</p> <p>22 "Adjustment for multiple tests."</p> <p>23 How many tests are being addressed</p> <p>24 there?</p> <p>25 A. In this example, it's 20.</p>
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<p>1 - STEPHEN D. PROWSE -</p> <p>2 way you've asked it. It just doesn't make any</p> <p>3 sense.</p> <p>4 Q. Okay. Now, let's go -- let's take</p> <p>5 a look at the Perneger article. It says -- and</p> <p>6 there's a number of points. See the blue?</p> <p>7 A. Yes.</p> <p>8 Q. That says "Adjusting Statistical</p> <p>9 Significance for the number of tests that have</p> <p>10 been performed on study data -- the Bonferroni</p> <p>11 method -- creates more problems than it</p> <p>12 solves."</p> <p>13 Do you agree or disagree with</p> <p>14 that?</p> <p>15 A. I disagree with that in the sense</p> <p>16 that this is an article designed pri -- it</p> <p>17 looks solely for biomedical research, where</p> <p>18 typically you have very, very large numbers of</p> <p>19 tests performed. And, therefore, the</p> <p>20 Bonferroni method may be more problematic</p> <p>21 there.</p> <p>22 But for the types of cases that I'm</p> <p>23 involved in or that don't involve those types</p> <p>24 of -- those numbers of tests. And, therefore,</p> <p>25 I think the Bonferroni method is perfectly</p>	<p>1 - STEPHEN D. PROWSE -</p> <p>2 Q. How many were you talking about?</p> <p>3 A. I'm talking about nine or 18</p> <p>4 regressions.</p> <p>5 Q. Okay. Well, this article is</p> <p>6 addressing nine -- I mean 20 trials.</p> <p>7 Is that a significantly larger</p> <p>8 number than the 18 or 19 that you conducted?</p> <p>9 A. This example isn't, but my</p> <p>10 understanding is that the literature talks</p> <p>11 about the Bonferroni adjust -- or correction</p> <p>12 being problematic when you have very large</p> <p>13 numbers of tests.</p> <p>14 Q. Well, doesn't this article talk</p> <p>15 about Bonferroni adjustments being problematic</p> <p>16 when there are 20 independent tests that are</p> <p>17 being performed?</p> <p>18 A. Well, I would have to read the</p> <p>19 whole article to understand it, but my</p> <p>20 understanding is that this is an article that's</p> <p>21 focused on biomedical research or epit --</p> <p>22 epitomology, not the types of issues that we're</p> <p>23 dealing with here.</p> <p>24 Q. What difference does it make if</p> <p>25 you're just talking about application of</p>

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<p>1 - STEPHEN D. PROWSE - 2 mathematical statistical analyses what -- what 3 you're looking at? 4 A. Well, one difference is that we're 5 looking at a universal null here. We're 6 looking at is there a pricing impact or not, 7 regardless of the channel? And this article 8 itself says that a Bonferroni adjustment may be 9 appropriate in those cases. 10 Q. Wait a minute. You're saying that 11 you're looking at is there a price impact or 12 not? 13 A. Yes. 14 Q. I thought what we were looking at 15 is could you reject the null hypothesis that 16 there was a price impact? 17 A. Fine. If you want to put it that 18 way, we're looking at a null hypothesis, 19 universal null, which is, is there a price 20 impact or not? Or is there a price -- the null 21 hypothesis being no impact. That's the 22 universal null that we're looking at. 23 We can test that in a number of 24 different ways. And that's -- that's what 25 we're doing here. There's no pre-established,</p>	<p>1 - STEPHEN D. PROWSE - 2 these -- 3 Q. Failing to reject the null when it 4 is false. 5 A. Yes, that's right. Yeah. Now 6 you've said it and I agree. It's very late. 7 Q. So, failing to reject the null. 8 Isn't that what the 15 regressions did in your 9 analyses here? 10 A. That's what all of the regressions 11 did. 12 Q. Well, 15 of the 18. Three of them 13 showed that there was a significant 14 correlation, which you indicated you think are 15 spurious. But 15 of them failed to reject the 16 null. Right? 17 A. I would disagree with that. I 18 would say all of them failed to reject the null 19 when you properly adjust for the spurious 20 correlation property. 21 Q. Okay. But if you do the 22 adjustment, okay, doesn't it increase the 23 likelihood of the results that the null 24 hypothesis has not been rejected? Does it 25 increase the error?</p>
<p>1 - STEPHEN D. PROWSE - 2 specific hypothesis about exactly how the 3 transmission mechanism would go from a Badian 4 or a Rhino trade to the Sedona stock price. 5 Q. What's the -- 6 A. And, therefore, so there's no 7 specific transmission mechanism. There's lot 8 of potentially different ones. 9 Q. Okay. What's a Type II error? 10 A. A Type II error is the opposite of 11 a Type I error. Type I error is rejecting the 12 null when it's true, and a Type II error is 13 failing to reject the null when it's false. 14 Q. Okay. And does the application of 15 the Bonferroni method increase the likelihood 16 of a Type II error? 17 A. It generally increases the 18 likelihood of a Type II error and decreases the 19 likelihood of a Type I error. 20 Q. And the Type II error being a 21 finding of no significance? 22 A. A Type II error is failing to 23 reject the null when it is -- I'm sorry. It's 24 very late. Failing to reject the null when it 25 is false. Yes. I got that right. There's all</p>	<p>1 - STEPHEN D. PROWSE - 2 3 A. No, what it does is it restores 4 the Type I error to the original Type I error 5 rate that you would expect from just running 6 one regression. You want to restore the Type I 7 error rate to 5 percent, and that's what the 8 Bonferroni correction does. 9 Q. Based on the use of regression 10 analyses that may generate a false result 11 themselves. 12 A. I don't know what you're talking 13 about. 14 Q. Well, isn't it true -- isn't it 15 true that any one of these regression analyses 16 could have resulted in a false result? 17 MR. SOHN: Objection to the 18 form. 19 A. I don't know what you mean by a 20 "false result." 21 Q. A false positive significance, a 22 false negative significance. 23 A. There's always an error of -- in 24 all statistics, there's always an error of a 25 false positive or a false negative. The generally accepted way of going about any kind</p>

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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 of statistical analysis is to set the Type I	2 analysis?
3 error at 5 percent, and that's what the	3 Q. Yeah, with regard to any
4 Bonferroni correction does when you're doing	4 particular regression. What does low power
5 multiple comparisons.	5 mean?
6 Q. The -- remember I asked you a	6 A. Low power means a higher level of
7 question about the powers of tests?	7 Type II error.
8 A. I believe so.	8 Q. And the Type II error being that
9 Q. Now, isn't it true that if you do	9 you find that you can't reject the null
10 a regression and you find the results are not	10 hypothesis when the null hypothesis should be
11 significant and the null hypothesis is not	11 rejected?
12 rejected, one of the reasons that this can	12 A. Failure to reject the null when
13 happen is because the null hypothesis is false,	13 the null is false, right.
14 but by chance the data happened to be of the	14 Q. Okay.
15 kind expected under the null hypothesis?	15 MR. SOHN: Mr. Guido, I think
16 A. That is certainly a possibility.	16 we've hit seven.
17 Q. If the power of the test is low,	17 MR. GUIDO: One more question.
18 is this more likely to be possible?	18 BY MR. GUIDO:
19 A. If the power of the test is low,	19 Q. Did you attempt to determine what
20 then the chances of a Type II error are higher,	20 the probability of accepting the false on a
21 yes, I believe.	21 null hypothesis was in any of your regressions?
22 Q. Okay. And if the study that has	22 A. Did I attempt to -- no. I mean, I
23 low power fails to show a significant effect,	23 attempted to fix the probability of a Type II
24 are the results more fairly described as	24 error at the generally accepted level.
25 inconclusive than as negative?	25 MR. GUIDO: Okay. No further
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1 - STEPHEN D. PROWSE -	1 - STEPHEN D. PROWSE -
2 A. I'm sorry, I missed that.	2 questions.
3 Q. When a study with low power fails	3 MR. SOHN: Mr. Guido, I just, you
4 to show a significant effect, are the results	4 know, expected that you will instruct your
5 more fairly described as inconclusive than	5 colleagues who are here today to maintain their
6 negative?	6 notes, whatever they've been writing.
7 MR. SOHN: Objection to the form.	7 MR. DUNBAR: Could we go off the
8 A. I'd have to think about that.	8 record? Is that really what you meant to say?
9 Q. Have you ever thought about it	9 MR. GUIDO: About the -- I'm
10 before?	10 sorry, Fred. You're not asking the questions.
11 A. Not exactly in those words, but --	11 THE VIDEOGRAPHER: This concludes
12 so I'd have to think about it.	12 the videotaped deposition of Dr. Stephen Prowse
13 Q. Well, when was the last time you	13 consisting of five videotapes. Going off the
14 read the Kaye-Freedman piece?	14 record at 6:56 p.m.
15 A. What piece are you talking about?	15 (Whereupon, the deposition
16 Q. The piece that you cited from	16 concluded at 6:56 p.m.)
17 the -- what is it? The section on statistics	17
18 from the -- from the judiciary.	18
19 A. Not -- certainly not within the	19
20 last few weeks or months.	20
21 Q. Well, did you read it when you	21
22 were preparing your report?	22
23 A. No. I was aware of it.	23
24 Q. What is a low power?	24
25 A. With regards to a statistical	25

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1 **CERTIFICATE OF DEPONENT**
 2 I hereby certify that I have read and examined the
 3 foregoing transcript, and the same is a true and
 4 accurate record of the testimony given by me.
 5 Any additions or corrections that I feel are
 6 necessary, I will attach on a separate sheet of
 7 paper to the original transcript.

8

9

10

11 _____
 12 Signature of Deponent

13

14 I hereby certify that the individual representing
 15 himself/herself to be the above-named individual,
 16 appeared before me this _____ day of _____,
 17 2010, and executed the above certificate in my
 presence.

18

19

20

21 _____
 22 NOTARY PUBLIC IN AND FOR

23

24 _____
 25 County Name

MY COMMISSION EXPIRES:

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1 **CERTIFICATE**
 2

3 I, Bridget Lombardozzi, Certified
 4 Shorthand Reporter and Notary Public, hereby
 5 certify that the foregoing is a true and
 6 accurate transcript of the deposition of said
 7 witness who was first duly sworn by me on the
 8 date and place hereinbefore set forth.

9

10 I FURTHER CERTIFY that I am neither
 11 attorney nor counsel for, nor related to or
 12 employed by, any of the parties to the action
 13 in which this deposition was taken and further
 14 that I am not a relative or employee of any
 15 attorney or counsel employed in this action,
 16 nor am I financially interested in this case.

17

18 Dated this 7th day of March, 2010.

19

20

21

22 _____
 23 Bridget Lombardozzi
 24 Certified Realtime Reporter - NCRA
 25 Certified Shorthand Reporter
 New York Notary Public

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